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ABSTRACT

This study examines the entitlement and payment arrangements set out in the maintenance and operations portion of the impact aid laws. Section 1 provides a brief background description of the program, including the changes made in the 1974 Amendments, a recent budget history, and a description of the program's beneficiaries. Section 2 contains an assessment of the major features of the program and the extent to which they achieve the program's objectives. Specifically, three major issues are addressed: Are school districts adequately compensated for federally imposed burdens? Are impact aid funds equitably distributed in terms of district needs and federal impact? Does impact aid interfere with state equalization programs? In Section 3 a variety of reform options are presented that address the problems described in Section 2. Each of these options is analyzed in terms of its ability to improve current practices. Section 4 combines several of the reforms of Section 3 into three comprehensive reform packages. These address specific reform goals and illustrate the effects of simultaneously changing several aspects of the program. (Author/IRT)

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Technical Analysis Paper 5

IMPACT AID TWO YEARS LATER

An Assessment of the Program as Modified by the 1974 Education Amendments

Lawrence L. Brown, III
Alan L. Ginsburg
Martha Jacobs

March 30, 1978

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Office of the Assistant Secretary for Planning and Evaluation -- The Education Planning Staff -- U. S. Department of Health, Education, and Welfare

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IMPACT AID TWO YEARS LATER -- AN ASSESSMENT OF THE PROGRAM AS MODIFIED BY THE 1974 EDUCATION AMENDMENTS

Technical Analysis Papers of the
Education Planning Staff

1. Patterns of Federal Aid to School Districts, Alan L. Ginsburg with J. N. Killalea, February 1975.

2. Education and Earnings: A Review of the Evidence, C. Russell Hill, May 1976.

3. Statistical and Policy Implications of the Education Amendments of 1974 (P.L. 93-380): A Post Mortem, Lawrence L. Brown, III and Alan L. Ginsburg, August 1976.

4. School Finance Reform in the Seventies: Achievements and Failures, Lawrence L. Brown, III, Alan L. Ginsburg, J. Neil Killalea, Richard A. Rosthal, and Esther O. Tron, September 1977.

5. Impact Aid Two Years Later: An Assessment of the Program as Modified by the 1974 Education Amendments, Lawrence L. Brown, III, Alan L. Ginsburg, and Martha Jacobs, March 1978.

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PREFACE

This study examines the entitlement and payment arrangements set out in Sections 3(a), 3(b), and 5 of P.L. 81-874, the Maintenance and Operations portion of the Impact Aid laws. The study was undertaken in the context of developing an Administration proposal for Impact Aid as part of the reauthorization of the Elementary and Secondary Education Act. In addition, requests that this type of study be conducted were made to Secretary Califano last summer by the Chairmen of the House Authorizing and Appropriations Committees which have jurisdiction over the program, as well as by Senators Bellmon and Muskie of the Senate Budget Committee. Finally, the availability of program data from FY 1976 made this an opportune time to assess the effects of reforms which were enacted in the Education Amendments of 1974, and first implemented in FY 1976.

This report was prepared by Lawrence L. Brown, Alan L. Ginsburg, and Martha Jacobs of the Office of the Assistant Secretary for Planning and Evaluation, Department of Health, Education, and Welfare (OASPE). Significant contributions, comments and criticisms were made by Michael O'Keefe, Deputy Assistant Secretary for Planning and Evaluation/Education Planning, and by Rob Barnes of the OASPE staff; William Stormer, Director, Division of School Assistance in Federally-Affected Areas/OE, and Edna Cave of the SAFA staff; Darrel J. Grinstead, Office of the General Counsel/Legislative Division/OS; William Dingeldein, Director, Division of Education Budget Analysis, Office of Assistant Secretary for Management and Budget/OS; A. Ray Peterson , Special Assistant to the Deputy Assistant Secretary for Legislation (Education)/OS; Joel Burke, Deputy Assistant Secretary for Education Policy Development, Office of the Assistant Secretary for Education/OS; and Jim Fox, National Institute of Education.

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EXECUTIVE SUMMARY

Introduction

Initiated in 1950, School Assistance for Federally Affected Areas (Impact Aid) was the first major Federal elementary and secondary education program. The Impact Aid program provides funds to compensate school districts for the cost of educating children when enrollment and availability of revenues from local sources are adversely affected by Federal activities. Over the years the Impact Aid program has been the object of much debate, several major studies, and numerous legislative proposals and amendments.

The present study was undertaken in the context of developing an Administration proposal for Impact Aid as part of the reauthorization of the Elementary and Secondary Education Act. In addition, requests that this type of study be conducted were made to Secretary Califano last summer by the Chairmen of the House Authorizing and Appropriations committees which have jurisdiction over the program, as well as by Senators Bellmon and Muskie of the Senate Budget Committee. Finally, the availability of program data from FY 1976 made this an opportune time to assess the effects of reforms which were enacted in the Education Amendments of 1974, first implemented in FY 1976.

This study examines the entitlement and payment arrangements set out in the Maintenance and Operations portion of the Impact Aid laws, specifically, Sections 3(a), 3(b), and 5 of P.L. 81-874. Section I (pp. 1-11) provides a brief background description of the program, including the changes made in the 1974 Amendments, a recent budget history, and a description of the program's beneficiaries.

Section II (pp.12-92) contains an assessment of the major features of the program and the extent to which they achieve the program's objectives. Specifically, three major issues are addressed:

- Are school districts adequately compensated for Federally imposed burdens?
- Are Impact Aid funds equitably distributed in terms of district needs and Federal impact?
- Does Impact Aid interfere with State equalization programs?

In Section III (pp. 72-136) a variety of reform options are presented which address the problems described in Section II. Each of these options is analyzed in terms of its ability to improve current practice. Also analyzed is each option's effect on total program costs, district participation, and the distribution of funds to districts classified by degree of Federal impact, metropolitan status, and property wealth.

Section IV (pp. 137-150) combines several of the reforms of Section III into three comprehensive reforms packages. These address specific reform goals and illustrate the effects of simultaneously changing several aspects of the program.

Highlights of the study follow.

Are School Districts Adequately Compensated for Federally Imposed Burdens?

The current program attempts to compensate for burden by providing payments for certain types of Federally connected children. Payments are based on a local contribution rate (LCR) which is intended to reflect the district's share of per pupil costs. The percentage of LCR to which a district is entitled varies for the different categories of Federal children and is intended to approximate the portion of local revenues lost to a district as a result of each child's Federal connection. Thus, in assessing the extent to which this arrangement adequately compensates for Federal burden, the study examines whether children for whom payments are made actually constitute a Federally imposed burden on a district. The study also assesses whether the methods used to calculate LCR and the weights assigned for entitlement purposes result in payments commensurate with the burdens imposed.

Federally Connected Children

Historically, critics of Impact Aid have charged that the program makes payments for some types of children who do not place a major burden on a district's ability to finance education. Even the strongest critics of Impact Aid acknowledge that "A" children who live and whose parents work on non-taxable Federal property, are associated with a clear tax loss to the school district.

However, no such concensus exists regarding "B" payments for children who live or whose parents work on Federal property. Payments for "B" category children often have been the subject of reform proposals. The most recent of these proposals would have reduced the FY 1978 Impact Aid budget by eliminating these payments entirely. The principal justification for this and

similar proposals rests on the observation that "B" children, most of whom live on taxable residential property, represent much less of a potential revenue loss to a district than "A" children, whose parents both live and work on non-taxable Federal property.

Four reform options are examined which would eliminate entitlements for particular categories of children:

- o Option 1 eliminates all entitlements for "B" children.
- o Option 2 eliminates all "B" entitlements except "B" military and "B" live-on children.
- o Option 3 eliminates entitlements for "B" students whose parents work outside the county of the school district.
- o Option 4 eliminates entitlements for public housing children (both "A" and "B").

The present study concludes that there are relatively strong justifications for providing payments for "B" children who are associated with some tax loss to the district. As a result, reform options which would eliminate payments for all or most types of "B" children are deemed overly harsh. Such options would result in large reductions in total program costs and would adversely affect both heavily and lightly impacted districts, wealthy as well as poor districts.

However, the justifications for "B" out-of-county and public housing children are not as persuasive. "B" children whose parents work on Federal property outside the county in which the school district is located are not associated with a tax loss to the school district. These children live on taxable residential property and the non-taxable Federal property on which their parents work is outside the school district.

Non-taxable public housing property is locally rather than Federally owned. The Federal government already provides substantial aid to the community through housing subsidies, debt service guarantees, and in lieu-of-tax payments. Moreover, compared with the ESEA Title I grants for disadvantaged, public housing payments are not effectively targeted on educationally needy children.

Eliminating "B" out-of-county payments would reduce total costs by about 5 percent and eliminate payments for 64 districts. Elimination of public housing payments would lower costs by over 10 percent, with payments for 43 districts totally eliminated. Reductions resulting from both the reform options are equitably distributed in terms of degree of Federal impact and property wealth, with lightly impacted and wealthy districts bearing the

brunt of reductions. However, the public housing reform results in disproportionately large reductions in center city districts.

Although these two reform options make sense in terms of Impact Aid objectives, they do have some drawbacks. In particular, the public housing reform would eliminate payments for children who are educationally disadvantaged, and in need of special services, and would have adverse effects on cities, whose current fiscal difficulties are well-known. Consequently, implementing this type of reform may well be impossible unless the legitimate claims of these children and their districts are addressed through increased efforts in programs like ESEA, Title I -- programs which are designed to deal more effectively with the real educational problems of these groups.

Local Contribution Rates

The Impact Aid program seeks to compensate districts for the portion of per pupil costs that would have been paid from local revenues had these not been lost or reduced as a result of Federal activity. Because there is no straightforward way of determining these amounts from a Federally impacted district's actual educational costs, the current law provides several alternative methods for calculating the local contribution rate. This rate may be either an estimate based on comparable districts of the agency's per pupil costs derived from local revenues, or alternatively, a minimum rate of one-half the State or national average per pupil costs.

This study identifies several major weaknesses in the current procedures for calculating local contribution rates. The comparable district method does not provide a good approximation of what local education costs would have been in the absence of Federal impact. In effect, it permits districts to select wealthy comparables on the basis of characteristics which are most likely to be affected by Federal presence. As a consequence, districts using this method obtain rates that are 40 percent higher than those they would receive using the higher of the two minimum rates. Wealthy districts rely on this method for over 50 percent of their Impact Aid funds.

The minimum rate of one-half the national average per pupil expenditures bears no relation to local education costs. In effect, it serves as a floor on payment rates. It addresses a concern which is really beyond the scope of the Impact Aid program -- the problem of inter-State expenditures disparities.

Reform options are examined which move away from the present practice of relying on biased or excessively inflated estimates of what district costs would be without Federal impact. They do

this by restricting or eliminating use of the comparable district and/or national average calculations and substituting in their place other methods based on the average revenue or expenditure patterns of individual States:

- o Option 1 restricts use of the comparable district method to high impact districts, and retains the two minimum rates.
- o Option 2 is the same as Option 1 except that the minimum rate of one-half national average expenditures is eliminated.
- o Option 3 sets a district's rate at either its State's average local expenditure per pupil or at one-half its State's average non-Federal expenditures per pupil, whichever is higher.
- o Option 4 guarantees each district its State average property base and determines the LCR by multiplying this base by the district's own revenue effort rate. This option also includes a minimum rate guaranteeing a district at least one-half State average non-Federal revenues.

Although none of these options is perfect, all achieve some measure of reform. Options 3 and 4 (which would reduce program costs by about 13 percent and 0.5 percent respectively) make the most reasonable assumptions about Federal impact, and both are relatively evenhanded with respect to different State finance systems. Options 1 and 2 do not measure up nearly as well on these criteria, probably because they both try to work with the current program's compensation mechanisms. Of the two, the second option makes the most reasonable assumptions about Federal impact and is most evenhanded. However, Option 2 is also the harshest of all the options, reducing total program costs by over 15 percent.

All options tend to be fairly progressive in their effects on districts classified by wealth. Districts which lose least (or gain) from reform are poor districts. Heavily impacted districts also tend to do better than other districts under these options. By far, those with the most to lose are high wealth districts and those moderately impacted. Districts in low expenditure/high State aid States (especially those in the South) also have much to lose from these LCR reforms.

Are Program Funds Equitably Distributed in Terms of District Wealth and Need?

A longstanding criticism of the Impact Aid program is that it distributes large amounts of money to affluent districts -- districts which may have benefited by Federal activity and which could easily support a high level of educational expenditure without Impact Aid. A related and perhaps more significant issue concerns the appropriateness of distributing scarce Federal dollars to lightly impacted districts.

Evidence indicates that there is substance to these criticisms. For example, nearly 20 percent of Impact Aid funds are paid to over 2,500 low impact districts with fewer than 10 percent Federally connected children. These funds represent a small portion -- on average, less than 2 percent -- of the local revenues available to those districts. Moreover, lightly impacted districts are generally at or above State average property wealth despite the presence of Federal acitvities.

In contrast, heavily impacted districts, with Federal enrollments of 50 percent or more, show real evidence of burden from Federal activity. These districts' property wealth is only about one-half their respective States' averages. Moreover, these districts are very much dependent on the Federal payments to finance their educational programs.

The data clearly indicate that lightly impacted districts are much less dependent on Impact Aid funds and could adjust to the elimination or reduction of these payments without suffering undue hardships.

Thus it is reasonable to conclude that in setting Federal funding priorities, heavily impacted districts, whose burdens are relatively unambiguous, are much more deserving of compensation than lightly impacted ones whose burdens are less apparent, or who may benefit from the Federal presence.

Several reform options were developed to improve targeting of Impact Aid funds on heavily burdened districts. The options are based on the concept that districts should "absorb" costs, that is, pay full costs of educating a minimum percentage of their Federally connected children.

- Option 1 extends the applicability and effect of the current law's absorption provision by removing the limitations imposed on the absorption.

- Option 2 requires that districts absorb costs of educating Federal students equal to a specified percentage of the non-Federal enrollment. Three, four, and five percent absorptions have been simulated. This option eliminates the need for the tier system.

The first option builds on a very limited absorption provision in the current law. This provision requires only lightly impacted districts to pay full costs for a small percentage (which cannot exceed 2 percent) of their "B" children. The first option would extend this absorption's applicability to all districts, and remove the limitations on the number and percent of children for whom costs are to be absorbed.

The first absorption option would reduce program costs by about 20 percent. Although all impact categories would experience reductions, losses are distributed progressively, with the low impact districts suffering greatest losses. Payments to 455 districts would be completely eliminated under this option.

The second absorption design applies to both "A" and "B" payments and is intended to adjust for the different burdens imposed by the various types of Federal children and for the relative degree of Federal impact on districts. This approach would require a district to assume the full costs for educating a number of Federal children equal to a specified percentage of the district's non-Federal average daily attendance. This option would also eliminate use of the tier system for prorating payments and assure payment at full entitlements for remaining children.

This option was simulated at 3, 4 and 5 percent absorption levels. These were selected because they provide a range of options and establish the principle that the Federal government's responsibility extends only to those districts with above average Federal impact (at least 3 percent of non-Federal children) and for such districts, only to the costs of educating students above that average. While reductions in total costs of about 7.5 and 19 percent are achieved by the 4 and 5 percent absorptions, the 3 percent absorption increases costs by about 6 percent. All three options increase payments to districts in the over 25 percent impact categories. They greatly reduce or eliminate payments to districts with less than 10 percent Federal children. Approximately 1,900 to 2,500 districts would be eliminated under these options.

Although all of the absorption reforms achieve some measure of success in reducing payments to lightly burdened districts, the burden-based reforms are the most successful at rechanneling these funds to districts which are heavily impacted. By eliminating the need for the tier system and the separate eligibility requirements they also achieve a considerable measure of program simplification and equity.

As a practical matter, however, the burden-based absorptions do have one major drawback. Specifically, their benefits are

achieved by eliminating many districts from the program, something the first option does not do. Indeed, in this respect, the first option is the most acceptable reform examined, even though it has few of the administrative and equity properties which recommend the three burden-based reforms. If saving districts is a major selection criterion, then retaining the current absorption without its restrictions is the most viable of these reform options.

Does the Program Interfere with State Equalization Programs?

A major criticism of the Impact Aid formula has been that it allocates assistance to districts in ways that disregard and can undermine State equalization programs. Currently, the law prohibits the vast majority of States from counting Impact Aid as local revenues when determining a district's share in a State aid program. There is an exception to this prohibition for highly equalized States. However, the tests for determining whether States are sufficiently equalized to qualify for this exception and count Impact Aid as local revenues are very restrictive and thus one can argue that they provide only a partial solution to coordination with State equalization aid.

Most States do not qualify for the exception provision, and Impact Aid may actually impede their ability to reduce disparities. Although most Impact Aid districts for which data were available rank in the lowest two quartiles of State and local revenues within their States, a significant number of districts appear in the top two quartiles and thus would have relatively high resource levels even without Impact Aid. Such districts receive 40 percent of Impact Aid funds paid to the sample of districts examined, and the effect of these payments is often to increase the distance between spending levels in these districts and their State's average.

The major criticism of Impact Aid from the standpoint of equalization relates not so much to what the program does, but what it fails to do. It fails to give some States an incentive to reform their finances. It fails to give States that have made a modest start toward equalization an opportunity to achieve further gains by offsetting payments to relatively wealthy districts.

Reform options are examined which relax present standards of equalization to permit increased State offsetting of Impact Aid payments:

- Option 1 extends the current exception provision to permit offsetting in proportion to how closely the State approximates Federal equalization standards.

- o Option 2 eliminates the Federal equalization tests and permits offsetting in proportion to the portion of each district's local revenues that is equalized under the State's program.

- o Option 3 retains the current provision and permits other States to offset payments to high wealth districts.

The three options differ in the extent to which they achieve various equalization-related goals. If the objective of reform is to ensure that the Impact Aid program remains neutral with respect to State equalization efforts, the second option, which would eliminate the strict qualifying tests and permit virtually all States to count Impact Aid payments, goes the furthest of the three options toward achieving that goal. To a lesser extent, the first option also is directed toward coordinating Impact Aid with the distribution of State aid. However, if one is most concerned with assuring that Impact Aid has the effect of increasing equalization, the third option, which considers the wealth of Impact Aid districts, would be preferable.

Equalization-related reforms of Impact Aid can exert only a modest influence on State finances since, nationally, Impact Aid payments amount to less than 2 percent of all current expenditures for public elementary and secondary education. Thus the importance attached to these proposals is largely based on principles of equity and policy concerns in the area of Federal/State/local cooperation. At the district level, specific reform options can have a substantial effect on certain high impact districts. At State and Federal levels, the fact that program dollars may be going in opposite directions must be a matter of policy concern, irrespective of the absolute magnitude of the amounts involved. For both of these reasons, equalization-related reforms are deserving of serious consideration.

Comprehensive Reform Options

The preceding discussion focused on the independent effects of various reform options designed to address problems presently besetting the Impact Aid program. In addition, several comprehensive reform packages were designed which illustrate what happens when a number of current program provisions are modified simultaneously to address the major issues raised in the report. These options are intended to improve the program's ability to equitably compensate districts for genuine Federal burden, and address six reform goals:

(1) The Federal responsibility should extend only to students who represent a genuine Federal burden on the district.

(2) Methods used to calculate payment rates should be as objective as possible to minimize the likelihood of abuse. Procedures which yield unbiased approximations of what local education expenditures or revenues would have been in the absence of Federal impact are to be preferred over others.

(3) Heavily impacted districts have a more valid, higher priority claim on scarce Federal resources than lightly impacted districts.

(4) Impact Aid payments should not interfere with State equalization programs.

(5) Program operations should be rationalized and simplified.

(6) Insofar as they occur, fund reductions from reform should be progressive in terms of district burden.

The reform packages are intended to demonstrate that major problems can be addressed in a variety of ways, not to present a set of definitive program reforms. Because they differ in terms of the number of districts they eliminate, their cost implications and the extent to which they depart from current practices, the three packages illustrate a range of plausible strategies for programmatic reform:

- Option 1 eliminates payments for "B" out-of-county children; restricts use of comparable district method to high impact districts and retains both minimum rates, removes limitations from the current absorption; and implements the wealth related equalization provision.

- Option 2 eliminates payments for "B" out-of-county and public housing children; restricts use of the comparable district method to high impact districts and eliminates the minimum rate of one-half national average per pupil expenditures; implements a 3 percent burden-based absorption and eliminates the tier system; and implements the wealth related equalization provision.

- Option 3 eliminates payments for "B" out-of-county and public housing children; sets LCR at the greater of the State average of locally raised expenditures per pupil or one-half State average expenditures per pupil; implements a 5 percent burden-based absorption and eliminates the tier system; and implements the wealth related equalization provision.

Option 1 represents the most modest departure from the current program. It achieves cost savings (28 percent reduction in "A" and "B" payments), but eliminates a smaller number of districts (1,012) than the other options. Reductions are progressive on districts grouped by Federal impact and property wealth, with least impacted districts and wealthier districts experiencing greater losses from the reforms.

However, some critics will argue that this option does not go far enough in adjusting for differential Federal burden in its use of the current absorption provision. In addition, the LCR reform is not a strong element of this option, since it retains the national average minimum which yields a poor approximation of local Federal burden.

Option 2 is an intermediate level reform both to the extent it departs from current practice and in terms of its effect on program costs (33 percent reduction). By eliminating public housing payments and implementing the 3 percent absorption, Option 2 accords low burden children and districts less importance than the first option. Elimination of the minimum rate based on national average costs represents an improvement over the local contribution rate reform in the first option. Although the State average minimum rate on which most districts would have to rely is not perfect, it conforms better than the other methods with what is known about State/local expenditure patterns. The effects of Option 2 are progressive on districts classified by degree of impact with highest impact categories experiencing slight gains in funding and the greatest losses occurring in the low impact grouping. Option 2 eliminates payments to over 2,400 predominately low impact districts. This option also distributes losses progressively across districts grouped by property wealth.

The third option achieves the greatest cost savings (about 43 percent), eliminates payments for the largest number of districts (nearly 2,800), and represents the most significant departure from the current program. As a result, it is likely to be the most controversial of the three reform packages. However, it does have some features which recommend it. For example, the local contribution rate reform in Option 3 represents a reasonable method for approximating local costs of educating the Federal students. It has the added advantage of being relatively straightforward and not subject to manipulation and abuse. In addition, the strong absorption reform serves to establish the principle that the Federal government's responsibility extends primarily to districts which are most heavily burdened by Federal activities. Like the first two options, Option 3 is generally progressive in its effects on districts classified by degree of Federal impact and by property wealth.

Overall, Options 2 and 3 generally do a better job than Option 1 of achieving the kind of reductions and redistributions that many Impact Aid critics seek. They also would greatly simplify program administration, primarily by eliminating the complicated tier system. However, they accomplish these changes by eliminating payments for many districts and as a result may be considered to be too drastic.

Summary

Several conclusions can be drawn regarding the pitfalls and problems confronting those who would attempt to improve the Impact Aid program's ability to equitably compensate for genuine Federal burden.

First of all, it is clear that Impact Aid reform directed toward achieving the goals set out above will reduce or eliminate payments for many districts. There is absolutely no way to accomplish meaningful reform and maintain the status quo, because the majority of current program recipients are not burdened significantly. Even the relatively modest Option 1 results in substantial reductions in funding and district participation.

A second lesson learned from this analysis is that reforms which seek to sharpen the program's ability to target on genuine Federal burden generally will have an adverse effect on some types of districts and children who have a legitimate claim on other categories of Federal assistance. For example, while center cities are not burdened in an Impact Aid sense and, hence, do poorly under all of the reforms, they do have other critical educational problems which need attention.

Similarly, although public housing children do not necessarily represent an appropriate Impact Aid concern, many are educationally disadvantaged, and thus have a valid claim on other types of Federal assistance. Because Impact Aid never has really been equipped to deal with these kinds of problems, other vehicles which can address these concerns need to be devised, or if such vehicles already exist, they should be exploited more effectively. Expecting Impact Aid to continue to do this kind of double and triple duty is unrealistic and inconsistent with both the program's principal purposes and the reform objectives set out here.

Finally, areas exist where further study is warranted. In particular, additional investigation of alternative methods for gauging the net effect of Federal activities on district resources would be most helpful. Such an investigation could result in more equitable compensation schemes than those explored here.

Further investigation of the types of children for whom payments are made is also needed. For example, the extent to which payments are made for children whose parents work on Federal property in another district but not in another county should be determined, since these payments are as difficult to justify as those which are made for out-of-county "B" children.

Last, more information is needed about the effects which more flexible Impact Aid equalization provisions will have on total district revenues. Since improved coordination between State equalization reform and Federal funding is a topic which transcends the Impact Aid program, research might have particularly large payoffs. It might even result in Federal programs which are designed to facilitate rather than undermine State reform efforts.

I. BACKGROUND

School Assistance for Federally Affected Areas (Impact Aid) was initiated in 1950 "...in recognition of the responsibility of the United States for the impact which certain Federal activities have on the local educational agencies in which those activities are carried on..."[1/] Enactment followed hearings and investigations which indicated that Federal activities placed a burden on some districts through an increase in enrollment and loss in local taxable property. Enactment was also in response to conditions existing in 1950 which have substantially changed since that time. The nation was undertaking a military build-up for the Korean War; there was virtually no other Federal aid available for elementary and secondary education; and States provided a smaller share of the costs of educating students than they currently provide.

The purpose of the Impact Aid program is to compensate local school districts for the cost of educating children when enrollment and availability of revenues from local sources are adversely affected by Federal activities. Impact Aid payments are made under two separate legislative authorities: P.L. 81-874 provides assistance to local school districts to defray current operating costs of educating children in impacted areas and P.L. 81-815 is designed to provide school districts with financial aid for school construction under specified conditions (e.g., for construction of urgently

1/ Section 1, P.L. 81-874.

needed school facilities in districts where new Federal activities have substantially increased school membership). Major and pinpoint disaster assistance is also provided under both laws. Since most Impact Aid is provided under P.L. 81-874 -- $770 million in FY 1978 compared with $30 million for construction -- and because the issues involved are extremely complex, this paper will be concerned only with P.L. 81-874.[1/]

Program Description

P.L. 81-874 is the closest approximation to general aid from the Federal government for elementary and secondary education, since Impact Aid funds become part of the general operating accounts of school districts and no special accounting of their use is required. The Education Amendments of 1974 (P.L. 93-380) incorporated two exceptions: (1) funds provided for handicapped children of military personnel and handicapped children living on Indian lands must be used to support special programs that meet the needs of these children; and (2) payments for children from public housing projects must be used for ESEA Title I-type programs which provide services and compensatory education for disadvantaged children.

The majority of P.L. 81-874 payments are made to eligible local educational agencies for two broad categories of children: "A" children, whose parents live and work on Federal

1/ To be completely accurate, our analysis will deal only with amounts distributed under Sections 3(a), 3(b), and 5 of the current law.

property and "B" children, who live or whose parents work on Federal property, but not both. Federal property is defined to include Indian lands and Federally subsidized low rent public housing. All children living on Indian lands are "A" children and most of the public housing children are "B" category students. A local educational agency is eligible for Impact Aid if 3 percent of its enrollment, or 400 students, live and/or have a parent who works on Federal property.

Impact Aid payments are made to local educational agencies on the basis of an entitlement. The entitlement is expressed as a percentage of an agency's "local contribution rate" and is intended to compensate for the burden imposed by the various types of Federally-connected children at a rate which approximates locally raised education costs. The local contribution rate may be based either on comparable districts' per pupil costs derived from local revenues, or alternatively, a minimum rate of the greater of one-half the State or national average per pupil cost.

The percentage of the local contribution rate to which an agency is entitled varies for over a dozen subcategories of Federally connected children within the broad "A" and "B" classifications. This reflects the notion that different types of Federally connected children impose differing degrees of burden on the districts. For example, the higher entitlements for "A" children (90-150 percent of the local contribution

rate, compared to 40-75 percent for "B" children) reflect the theoretically greater loss in revenue to districts associated with the loss of tax revenues for both the place of residence and the place of work.

Within the "A" and "B" classifications the highest entitlements are provided for military and Indian handicapped children, reflecting the greater expense of providing an appropriate education for these children. Military children also receive relatively higher entitlements than civilians to compensate for the somewhat greater loss of revenues to a community which may result because military personnel often do business on the base rather than in the community and may be exempted from certain State or local taxes where they are stationed. Finally, within the "A" category, higher entitlements are provided for districts which are more heavily impacted -- i.e., where 25 percent or more of the district's enrollment are Federal children.

In addition to the payments for Federally connected children, special provisions authorize Impact Aid to school districts having a partial loss of tax base as a result of the removal of real property from the tax rolls through Federal acquisition (Section 2, P.L. 81-874); for districts experiencing a sudden and substantial increase of children resulting from Federal activities (Section 4); and for districts to receive an amount for a reduction in Federally connected children by

cessation or decrease of Federal activity (Section 3(e)). Finally, Section 6 of P.L. 81-874 authorizes payments to local education agencies and other Federal agencies to operate schools when local educational agencies are unable to provide a suitable free public education for Federally connected children. Given the size and complexity of the issues surrounding Sections 3(a), 3(b), and 5, evaluations of the program's special provisions have not been included in this paper.

History of Impact Aid Reform

While the basic structure and purpose of the Impact Aid program have remained intact since its enactment in 1950, the program has been amended numerous times over the years. The effect of these amendments has been to increase the local contribution rate for some districts and to expand the coverage of the program by broadening definitions of Federal lands and types of Federally connected children and by liberalizing eligibility requirements.

Perhaps the most extensive reforms were enacted in the Education Amendments of 1974. A significant feature of the 1974 reforms was the introduction of the "tier system" which directs the way entitlements will be pro-rated when the program is less than fully funded, and assures that payments will be made for public housing children. Although public housing children had previously been eligible for funding, special earmarking of appropriations was necessary to make these payments, and Congress never provided monies for this purpose.

The law requires that payments be made in three stages or "tiers":

- In Tier 1, payments are made at 25 percent of entitlement for all categories of children, including public housing children.

- In Tier 2, the various subcategories are prioritized: "A" payments are made at rates ranging from 88 percent to 100 percent of entitlement (including the amount paid under Tier 1). Total "B" payments in the second tier range from 53 percent to 60 percent of entitlement. No additional payments are made in Tier 2 for public housing children, so public housing payments remain at 25 percent through the second tier. If there are not enough funds appropriated to completely fund Tier 2, no payments in Tier 2 may be made. In this event, payments would be made through Tier 1 and through the hold harmless provisions which will be described later in the paper.

- In Tier 3, all remaining entitlements are paid. Payments for public housing children account for most funds paid in the third tier.

The 1974 reforms also eliminated or reduced entitlements for some "B" children. For example, "B" children whose parents work outside the State in which the local educational agency is located were eliminated as eligible Federally connected children. Similarly, entitlements were lowered for "B" children whose parents work outside the county in which the local educational agency is located. These changes were based on the argument that because the parents of these children pay residential property taxes, and because the tax loss from the non-residential property occurs outside the county or State of the agency, there is little or no burden on the agency.

Table 1 provides a description of each of the categories of "A" and "B" children. It also indicates their corresponding entitlement weights as well as their funding levels in each tier. The variations in entitlements are intended to reflect the relative burden associated with each category of child, while the funding levels assigned in the Tier system indicate priorities for payment among the categories.

Another provision in the reforms affecting "B" students is the requirement that, beginning in 1978, some school districts must assume the entire cost of educating a small percentage of their "B" students. This "absorption" provision does not apply to heavily impacted districts.

The 1974 reforms also included a change in the role of Impact Aid with respect to State educational aid programs. Under Section 5(d) States are prohibited from counting Impact Aid payments as local revenue in determining an agency's eligibility for or share in a State aid program. The reforms added a waiver to this prohibition for States which have a program to equalize educational expenditures among districts.

Finally, a major feature of the 1974 reforms was the inclusion of four "hold harmless" provisions to limit reductions in Impact Aid payments. In addition to a general hold harmless which applies to any reductions in payments, there are three others directed at specific reforms or conditions. One of these limits reductions resulting from the

Table 1. Fifteen Categories of Federally-Connected Students with Corresponding Entitlements and Payment Rates Under the Tier System

Section of P.L. 874	Description	Entitlement (Percent)	Percent of Entitlement Paid in Each Tier		
			Tier 1	Tier 2	Tier 3
3(a)	"A" CHILDREN -- Parents work and live on Federal property.				
3(a)(1) & (2)	"A" CHILDREN IN HEAVILY IMPACTED DISTRICTS -- Military and civilian "A" children whose school district contains 25% or more "A" children.	100	25 (25)	75 (100)	0 (-)
3(a)(1)	CIVILIAN "A" CHILDREN IN OTHER DISTRICTS -- Civilian "A" children in districts that are not heavily impacted.	90	25 (22.5)	63 (79.2)	12 (90)
3(a)(1)(LRH)	CIVILIAN "A" CHILDREN IN PUBLIC HOUSING -- Children whose parents live and work on Public Housing property.	90	25 (22.5)	0 (22.5)	75 (90)
3(a)(2)	MILITARY AND INDIAN "A" CHILDREN IN OTHER DISTRICTS -- Children whose parents live and work on Federal property or Indian Lands. Non-Indian children have parents in the uniformed services. School district is not heavily impacted.	100	25 (25)	65 (90)	10 (100)
3(a)(2)(LRH)	MILITARY "A" CHILDREN IN PUBLIC HOUSING	100	25 (25)	0 (25)	75 (100)
3(a)(2) Handicapped (25% or more)	HANDICAPPED MILITARY AND INDIAN "A" CHILDREN IN HEAVILY IMPACTED DISTRICTS	150	25 (37.5)	75 (150)	0 (-)
3(a)(2) Handicapped (Less than 25%)	HANDICAPPED MILITARY AND INDIAN "A" CHILDREN IN OTHER DISTRICTS	150	25 (37.5)	65 (135)	10 (150)
3(b)	"B" CHILDREN -- Parents work or live on Federal property, but not both.				
3(b)(1)	CIVILIAN "B" CHILDREN WHO RESIDE ON FEDERAL PROPERTY -- Children with civilian parents who live but do not work on Federal property.	45	25 (11.25)	32 (25.65)	43 (45)
3(b)(1)(LRH)	CIVILIAN "B" CHILDREN WHO RESIDE ON PUBLIC HOUSING PROPERTY -- Civilian "B" children whose parents live but do not work on public housing property.	45	25 (11.25)	0 (11.25)	75 (45)
3(b)(2)(A)	CIVILIAN "B" CHILDREN WHOSE PARENTS WORK ON FEDERAL PROPERTY IN THE COUNTY OF THE DISTRICT WHERE SCHOOL IS ATTENDED	45	25 (11.25)	32 (25.65)	43 (45)
3(b)(2)(A)(LRH)	CIVILIAN "B" CHILDREN WHOSE PARENTS WORK ON PUBLIC HOUSING PROPERTY IN THE COUNTY OF THE DISTRICT WHERE SCHOOL IS ATTENDED	45	25 (11.25)	0 (11.25)	75 (45)
3(b)(2)(B)	CIVILIAN "B" CHILDREN WHOSE PARENTS WORK ON FEDERAL PROPERTY IN THE STATE BUT NOT IN THE COUNTY OF THE DISTRICT WHERE SCHOOL IS ATTENDED	40	25 (10)	28 (21.2)	47 (40)
3(b)(2)(B)(LRH)	CIVILIAN "B" CHILDREN WHOSE PARENTS WORK ON PUBLIC HOUSING PROPERTY IN THE STATE BUT NOT THE COUNTY OF THE DISTRICT WHERE SCHOOL IS ATTENDED	40	25 (10)	0 (10)	75 (40)
3(b)(3)	MILITARY "B" CHILDREN -- Children whose parents are in the uniformed services and who either live or work on Federal prope	50	25 (12.5)	35 (30)	40 (50)
3(b)(3) Handicapped	HANDICAPPED MILITARY "B" CHILDREN	75	25 (18.75)	35 (45)	40 (75)

changes for out-of-county and out-of-State "B" children. Another partially offsets reductions in payments for other categories of children resulting from the funding of public housing children. There is also a hold harmless to prevent large losses in payments as a result of specific military base closings.

Budget History

Table 2 shows entitlements, budget requests and appropriations over the last eight years for the Impact Aid program (P.L. 81-874). Controversies over Impact Aid have tended to develop a pattern that is evident in Table 2: Presidents have annually proposed changes that would greatly reduce program costs; affected districts have testified that the changes proposed would cause cutbacks in their educational offerings; and the Congress has subsequently appropriated substantially larger amounts than requested by the Executive Branch.

It is important to note the relationship between entitlements under the program and the amounts which have been appropriated. Prior to fiscal year 1970, enough funds were appropriated to permit payment of full entitlements. However, since then, even though Congress has appropriated much larger amounts than were requested by the President, it has not fully funded the program. The "tier system" which went into effect in FY 1976, explicitly directs how payments will be made at

Table 2. Recent History of Entitlements,[a] Budget Requests and Appropriations for the Impact Aid Program (P.L. 81-874)

Fiscal	Entitlements[a]	Request	Appropriations	Difference Between Request and Appropriations
1970	$ 597,500,000	$187,000,000	$504,500,000	+ 317,500,000
1971[b]	897,200,000	410,000,000	536,068,000	+ 126,068,000
1972	924,000,000	425,000,000	592,580,000	+ 167,580,000
1973	976,000,000	415,000,000	635,495,000	+ 220,495,000
1974	979,391,000	273,500,000	574,416,000	+ 300,916,000
1975	1,053,500,000	320,300,000	636,016,000	+ 315,716,000
1976[c]	988,900,000	426,226,846	739,000,000	+ 312,773,154
1977	1,115,100,000	315,000,000	768,000,000	+ 453,000,000
1978	1,185,450,000	370,000,000	770,000,000	+ 400,000,000

a/ Excludes disaster assistance and hold harmless provisions.
b/ Public housing children eligible, although no appropriations made for them until FY 1976.
c/ Reforms enacted in the Education Amendments of 1974 became effective in FY 1976.

less than full funding. Congressional policy since the introduction of the tier system has been to fund the program through Tiers 1 and 2. In FY 1976 the amount appropriated was more than was needed for Tier 2 (although the intent was to fund only through Tiers 1 and 2), and, as a result, some payments were made in Tier 3. In FY 1977 and FY 1978 the appropriations law specifically directed that payments be made through Tiers 1 and 2 only.

The 1974 reforms also had the effect of lowering entitlements in FY 1976. However, due to increased claims for low rent housing payments and rising local contribution rates, entitlements in FY 1977, the second year of reform, were already above "pre-reform" levels. Thus, despite the enactment of reforms and some initial lowering of entitlements, appropriations have steadily increased since 1974. If the FY 1978 Congressional policy of funding Tiers 1 and 2, and two of the hold harmless provisions is continued, it is estimated that program costs will be over $1 billion by 1982.

Program Beneficiaries

In 1978 it is estimated that awards will be made to nearly 4,400 school districts on the basis of about 2.5 million Federally connected children. This includes payments made under Section 6 for other Federal agencies which maintain schools (primarily the Department of Defense). Since the majority of these funds are available for the general operating accounts of school districts, some or all of the 23 million children enrolled in Impact Aid school districts could conceivably benefit from the aid provided by the program. The fact that this is a general aid program and the relative lack of strings attached to the funds make this a very popular program with recipient districts.

II. EVALUATION OF CURRENT PROGRAM

Since its enactment nearly 30 years ago, the Impact Aid program has been the object of much debate, numerous legislative changes, and several major studies. The most extensive assessments of the program include a 1965 evaluation conducted by the Stanford Research Institute, a 1969 study by the Battelle Memorial Institute, and a 1976 report by the General Accounting Office.

Both the SRI and Battelle evaluations concluded that the basic structure of the program -- providing payments for Federally connected children and distinguishing between "A" and "B" children -- is defensible and properly conceived in terms of relieving burdens imposed on school districts. However, both of these studies, as well as the GAO report, identified aspects of the program which limit its effectiveness in compensating for these burdens. For example, the Battelle study found that Impact Aid results in unjustified overcompensation to many school districts. These Impact Aid "windfalls" are the result of payments which far exceed the Federally imposed burden. The payments are either in excess of the costs of educating the Federal pupils or do not reflect economic benefits that Federal activities may cause in a community. In addition, Battelle concluded that payments are made to wealthy school districts which could finance higher-than-average school costs without Impact Aid.

All of these studies were based on data collected prior to FY 1976, when the extensive reforms contained in the Education Amendments of 1974 were implemented. Using FY 1976 "post-reform" data this section will address the following major issues which have been raised by these studies as well as by the critics and proponents of the program:[1/]

- Are school districts adequately compensated for Federally imposed burdens?
- Are Impact Aid funds equitably distributed in terms of district needs and Federal impact?
- Does Impact Aid interfere with State equalization programs?

1/ The evaluation of the current program in this section and the simulations of reform components examined in subsequent sections were undertaken using several hybrid data files. SAFA payments for school districts, obtained from the Office of Education's FY 1975 and FY 1976 program tapes, were combined with specially gathered school district property value data for 1974-1975. Where necessary, the SAFA and property data were matched and merged with income and metropolitan status data derived from the 1970 Census Fifth Count File reaggregated to 1975-1975 school district boundaries. Some analyses required the combination of SAFA and these other data with information contained on NCES's 1974-1975 ELSEGIS finance file. Because a complete 100 percent match among all data sets was never possible (although match rates were generally in the 75-85 percent range), SAFA payment data displayed for "matched" variables like property wealth are incomplete and generally will not add to program totals. This is especially the case for small districts with enrollments of 300 or less and/or populations under 1,000. This attrition of districts and associated data should be kept in mind when interpreting the results of the study. Of necessity, some analyses are based on systematically constructed samples and generalizations must be made with caution.

Are School Districts Adequately Compensated for Federally Imposed Burdens?

Much of the controversy over the Impact Aid program has revolved around the issue of how well the program is compensating school districts for Federally imposed burdens. Although the burden concept is the basis for Impact Aid payments, identification and measurement of this burden has proven illusive. For example, in most instances, it is virtually impossible to determine what an area would have been like in terms of its revenue raising capacity and population without Federal activity. While it is true that in some areas the Federal government's activities have precluded private development which would have given rise to sizable local revenues, it is also true that in other areas the Federal presence has stimulated more economic activity and led to the creation of more taxable property than otherwise would have existed. The problem is that there is no generally accepted method for distinguishing between these two types of situations and for quantifying net tax losses or benefits to a district. The Battelle study, in fact, concluded that there is no feasible way to design a perfect procedure for Impact Aid that accurately measures the net burden of Federal installations.

The current program attempts to compensate for burden by providing payments for certain Federally connected children. Payments are based on a local contribution rate (LCR) which is intended to reflect the district's share of total per pupil

costs. The percentage of the LCR to which a district is entitled varies for the different categories of Federal children, and is calculated to approximate the portion of the LCR lost to a district as a result of each child's Federal connection. The following discussion examines this compensation arrangement. Specifically, it attempts to assess whether the children defined as Federally connected really do impose a Federal burden on a district and whether the methods used to calculate LCRs and the weights assigned for entitlement purposes result in payments commensurate with the burdens imposed.

Federally Connected Children

Historically, critics of Impact Aid have charged that the program makes payments for some children who do not place a major burden on a district's ability to finance education. Although the 1974 reforms eliminated entitlements for out-of-State "B" children, most past changes have been in the opposite direction and have expanded, rather than limited, program coverage. As a result, districts continue to receive payments for several categories of children who arguably do not represent a Federal burden on school resources.

Even the strongest critics of Impact Aid agree that "A" children are associated with a clear loss of tax base to school districts which must provide educational services for them. And there is no question that the loss of tax base and the

presence of these additional children result from Federal activities in the community. Consequently, reform proposals leave "A" payments (which will total nearly $300 million in FY 1978) untouched.

Payments for "B" category children, however, have been the focus of much criticism and the subject of numerous reform proposals. The most recent of these proposals would have reduced the FY 1978 Impact Aid budget by an estimated $345 million by eliminating these payments entirely. The principal justification for this and similar proposals rests on the observation that "B" children, most of whose parents live on private property and pay residential property taxes, represent much less of a potential revenue loss to a district than "A" children, whose parents both work and live on Federal property.

Because there are relatively strong justifications for payments based on some types of "B" children, total elimination of "B" payments seems an overly harsh measure. For example, about $90 million will be paid in FY 1978 for approximately 400,000 military "B" children whose parents are exempt from certain State and local taxes. Similarly, payments are made for other "B" children whose parents either work or live on non-taxable Federal property located within the school district. It would be difficult to deny that these children are not associated with at least a partial tax loss to the school district.

On the other hand, if one agrees that the major purpose of the Impact Aid program is to provide an in-lieu-of-tax payment for districts that have suffered some tax revenue loss through Federal presence, logic alone leads one to question the appropriateness of providing payments for some categories of children. In particular, the justifications for providing payments for "B" children whose parents work outside the school district, and for public housing children warrant close scrutiny.

Out-of-County and Out-of-District "B" Children

Originally, the Impact Aid program did not distinguish between children whose parents work inside and those whose parents work outside the district. However, since tax loss is the major feature of the burden concept, such a distinction is important. In particular, it can be argued that children whose parents work on Federal property outside the school district do not represent a Federal burden because, even if this property were taxable, the district would not benefit since it could not tax property beyond its boundaries.

The 1974 Amendments addressed this problem by eliminating the entitlement for children whose parents work on out-of-State Federal property and by reducing the entitlement for out-of-country "B" children. Critics argue, however, that these reforms did not go far enough, and should be extended to

eliminate out-of-county and out-of-district "B" payments as well. They contend that in terms of a district's ability to tax property, the most relevant boundary is the district boundary, not the State boundary, and they point to the fact that out-of-county "B" children will account for nearly $40 million in FY 1978 Impact Aid payments.1/

Justifications for including out-of-county and out-of-district "B" children as eligible Federal children emphasize that there may be a service burden on districts which must educate these children. This may occur when there is a large Federal installation "just across the district line" that attracts large numbers of civilian and military personnel whose children must be served. To the extent that property and other tax revenues resulting from these children (and the indirect economic benefits generated by the Federal government's presence) are less than enough to offset the increased costs of educating the Federally connected children, these districts will be adversely affected. The Battelle Study concluded that although payments should be less than for other

1/ Actual payments for out-of-district "B" children are likely to be much higher than $40 million. However, estimates are not available for payments which will be made for children whose parents work outside the district but within the same county, nor for hold harmless payments offsetting reductions in out-of-county and out-of-State "B" payments resulting from the 1974 reforms.

types of "B" children, all out-of-district payments, including out-of-State payments, can be justified on the basis of a service burden concept.

Many have challenged this conclusion asking why Federal sector activities outside a district should be more burdensome and deserving of compensation than private sector activities. After all, they argue, a large manufacturing plant or other private business usually would not be required to compensate an adjacent district just because it employed parents of children attending schools in that district.

Generally, we would agree that the arguments for including "B-out" children are not very compelling and question whether they warrant annual Impact Aid expenditures of over $40 million. These payments cannot be justified as compensation for tax loss, since the district would not be able to tax even private property outside its jurisdiction. Further, we would argue that many of these districts have been benefited rather than burdened by Federal activities. The benefits in these cases are expanded employment, commercial activities, and private residential tax base.

Public Housing Children

Since 1971, payments have been authorized for children whose parents live and/or work on Federally subsidized public housing property. However, until the Education Amendments of 1974, special earmarking of appropriations would have been required to make these payments, and monies were never provided for this purpose.

The Education Amendments changed this by including public housing payments in the tier system to assure that these payments would be made. In addition, the Amendments included the requirement that public housing payments be used specifically to provide educationally disadvantaged children with ESEA Title I-type compensatory education services. Although payments for public housing children are funded at the lowest rate through Tier 2 (25 percent of entitlement versus 53-100 percent for other categories), they will account for approximately $80 million in FY 1978.

Public housing property differs from other property which gives rise to Impact Aid payments in that public housing is locally, rather than Federally, owned. Despite this difference, proponents of public housing payments contend that the Federal government has a responsibility to offset district tax revenue losses which result when non-taxable public housing units are constructed. This responsibility is thought to stem from the role the Federal government plays in encouraging communities to construct the public housing. By participating in the program, a community often suffers a loss of tax base, but at the same time must provide educational and other services for a population which may well be in need of relatively higher cost services.

In response to the argument that public housing children impose a Federal tax burden, critics of these payments note

that public housing children are not, strictly speaking, Federally connected. The owners of public housing are local housing authorities, not the Federal government. Furthermore, these projects have been constructed in response to local government decisions under ground rules that were known in advance to them. Thus, critics conclude that public housing is not imposed on a local area by the Federal government.

It can be argued also that public housing payments may represent a duplication of Federal funding efforts. In addition to Impact Aid, the Federal government shares in the initial cost of building public housing units, guarantees debt service on bonds issued by local housing authorities, and makes annual contributions which subsidize payments in lieu of taxes. In FY 1976 disbursements to local housing authorities for public housing amounted to over $1.3 billion. It should also be noted that public housing authorities and local governments derive an indirect benefit through the lower interest rates made possible by Federal guarantees.

Proponents of public housing also claim that public housing creates a service burden for the district by drawing pupils into the community who would not otherwise be there. However, this argument can also be challenged. Because of long waiting lists in many communities and the need to be a community resident to get on these lists, public housing usually cannot draw persons to a community who would not otherwise be there. Typically, public housing serves existing community residents.

Finally, a major aspect of the justification for public housing payments is that they help districts offset the costs associated with high-need, educationally disadvantaged children. Unlike most other Impact Aid payments, public housing payments are not general aid but must be used to fund ESEA Title-I type compensatory programs. The main reply to this claim rests with evidence that, compared to Title I, the program does a poor job of channeling funds to areas with large concentrations of educationally needy children. The Title I formula is designed to allocate funds on the basis of poor children, on the grounds that poverty is an indicator of educational need. Thus, if Impact Aid public housing payments are being targeted effectively, one would expect their distribution to correspond to the distribution of children living in poverty. In fact, however, there is very little relationship between per pupil public housing payments and percent poor. This is in sharp contrast with the Title I program, which is highly targeted on the disadvantaged.

Additional evidence indicating that public housing payments are poorly targeted on the disadvantaged is provided in Table 3, which compares the rates at which the 16 largest center city districts receive Impact Aid public housing payments and ESEA Title I funds. Again, if public housing payments in these cities were targeted on need, one would expect their distribution to be similar to that of Title I

Table 3. Comparison of SAFA Public Housing and Title I Allotments Per Pupil for Sixteen Cities Ranked by Percent Title I Eligibles

Cities	Percent Title I Eligibles (1)	SAFA Public Housing Dollars Per Child 5-17 (2)	Title I Dollars Per Child 5-17 (3)
Washington, D.C	32.1	6.94	73.03
San Antonio	31.9	3.21	48.38
New York City	30.4	10.10	73.51
Detroit	29.5	0.99	63.08
Boston	29.4	2.40	55.15
Baltimore	28.7	0.75	62.82
Chicago	28.1	5.97	57.60
Philadelphia	26.8	5.17	57.38
Cleveland	24.2	2.68	42.11
San Francisco	19.7	1.53	36.32
Los Angeles	18.9	1.10	35.94
Dallas	18.9	2.06	28.77
Houston	18.6	0.44	28.19
Milwaukee	18.5	1.29	38.46
Indianapolis	15.6	0.89	26.42
San Diego	14.5	0.22	26.27

SOURCE: 1976 SAFA and Title I Program Data Files.

funds. However, Table 3 indicates that they are not similarly distributed. For example, while Baltimore and Chicago have about the same percentage of disadvantaged children and receive comparable Title I payments, they receive public housing payments at very different rates. In effect, it would appear that public housing payments are targeted on needy children only to the extent that these children live in cities with active, aggressive housing authorities.

In our view, inclusion of public housing children as eligible Impact Aid students is not consistent with the program's goal of providing compensation for Federally imposed burdens. Further, these payments do not provide an equitable distribution of funds to aid educationally needy children. This assessment does not deny that public housing payments provide some services for these children, nor does it deny the importance of the Federal role in assuring educational opportunities for disadvantaged pupils. The point is that the Impact Aid program is simply not an appropriate or effective vehicle for implementing this Federal responsibility.

Methods Used to Calculate Local Contribution Rates

The Impact Aid Program seeks to compensate school districts for the portion of per pupil costs that would have been paid from local revenues had these not been lost or reduced as a result of Federal activity. There is no straightforward

way of determining these amounts from a Federally impacted district's actual educational costs because these financial characteristics are clearly influenced by the presence of Federally connected children. Hence, the current law provides that a district's rate of compensation (i.e., its local contribution rate, or LCR) be based on the amounts private property owners in generally comparable districts pay toward the cost of educating children.

In practice, there are two procedural options from which a State may choose when using the comparable district method for determining LCRs. It may categorize all of its districts into several generally comparable groups and base each applicant's payment on its group's average per pupil expenditure from local revenues. Alternatively, rates may be based on an individual applicant's selection of at least five other comparable districts. In this instance, the SAFA district's LCR is based on these five comparable districts' average per pupil expenditures from local sources. The second procedure generally gives the Impact Aid district more latitude in determining its payment rate because the applicant can either make its own selection of the five districts to which it is compared, or do so in consultation with the State Education Agency.

Because the comparable district method can result in very low LCR's in States that finance a high percentage of

education from State sources (and/or States that have very low educational expenditures per pupil), the law also establishes a minimum payment rate which is the greater of either one-half the national or State average per pupil operating expenditures from non-Federal sources. This minimum rate is constrained in that it may not exceed the State average expenditure per pupil.

The extent to which the minimum and comparable district methods were used in 1976 is shown in Table 4 below. As the table shows, over half the districts we examined relied on the minimum method which guarantees at least one-half the national average expenditure per pupil. The next most popular method was one or the other of the two comparable district procedures (about 25 percent of all districts selected a comparable district procedure). Only about 18 percent of all districts relied on the minimum of one-half the State average expenditures.

These figures reveal nothing about the different cost impacts of using the various methods. Indeed, in this respect the results are somewhat misleading. In particular, although only about 25 percent of all districts choose one or the other comparable district procedures, over 37 percent of all program dollars are allocated to districts using this method. About 49 percent of all funds are targeted on districts using the national average method, while only about 14 percent of all funds go to districts that choose the State average minimum.

The method chosen by a district depends in large part on how its State finances education. For example, Table 4 suggests that the comparable district method will be chosen by districts in States which rely heavily on locally raised revenues to support education. On the other hand, districts in States which share a large portion of total education costs generally rely heavily on one or the other minimum calculation methods. Whether a district selects the State or national minimum clearly depends on which method will maximize its grant. Thus, where a State's average expenditure is greater than the national average, the State average minimum will be selected. Where the opposite is true, the national minimum will be chosen.

Finally, the last column in table 4 shows that, as one might have guessed, variations in the methods used to calculate local contribution rates result in substantial interstate differences in average LCR. In general, States with high average LCR's tend to be those which rely heavily on locally raised revenues to support education. These include New York, New Jersey, New Hampshire, Connecticut, Oregon, and Massachusetts. States with low average LCR's are most often those with low overall levels of support for education and/or those which rely heavily on State rather than local revenues. These include Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, and Mississippi. Most are Southern or border states.

Table 4. Number of Districts by State and Type of Local Contribution Rate: 1976[a/]

State	Total Districts in Sample (1)	Number of Districts Using: Comparable District LCR[b/] (2)	1/2 State Average LCR (3)	1/2 U.S. Average LCR (4)	Average LCR Per SAFA Pupil (5)
* Alabama	85	--	--	85	$ 569.73
* Alaska	29	1	28	--	1,582.59
Arizona	107	22	--	85	580.10
* Arkansas	97	--	--	97	569.73
California	465	70	--	395	589.62
Colorado	86	15	--	71	635.09
Connecticut	34	15	19	--	860.06
* Delaware	5	--	5	--	656.24
District of Columbia	1	--	1	--	760.69
* Florida	26	--	--	26	569.73
* Georgia	79	--	--	79	569.73
* Hawaii	1	--	1	--	$ 639.54
Idaho	68	3	--	65	571.15
Illinois	165	26	139	--	832.00
Indiana	48	1	--	47	575.02
Iowa	37	37	--	--	574.94
Kansas	74	74	--	--	598.21
* Kentucky	65	--	--	65	569.73
* Louisiana	21	--	--	21	569.73
Maine	68	--	--	68	569.73
Maryland	18	9	9	--	785.33
Massachusetts	125	77	48	--	$ 748.13
Michigan	63	5	58	--	680.73
* Minnesota	44	--	44	--	640.57
* Mississippi	36	--	--	36	569.73
Missouri	142	67	--	75	597.06
Montana	127	51	--	76	651.76
Nebraska	27	27	--	--	765.68
Nevada	14	--	--	14	569.73
New Hampshire	42	38	--	4	915.53
New Jersey	169	158	11	--	1,058.94
* New Mexico	62	--	--	62	$ 569.73
New York	160	31	129	--	1,305.58
* North Carolina	64	--	--	64	569.73
North Dakota	67	--	--	67	569.73
Ohio	115	45	--	70	676.68
* Oklahoma	341	10	--	331	570.97
Oregon	88	81	7	--	853.37
* Pennsylvania	107	28	79	--	710.45
Rhode Island	19	13	6	--	744.11
* South Carolina	23	--	--	23	569.73
South Dakota	51	51	--	--	$ 664.28
* Tennessee	92	--	--	92	569.73
* Texas	246	4	--	242	574.71
* Utah	35	--	--	35	569.73
Vermont	17	6	--	11	621.04
Virginia	65	10	--	55	711.64
* Washington	160	16	144	--	590.59
* West Virginia	12	--	--	12	569.73
Wisconsin	47	47	--	--	655.38
Wyoming	25	14	11	--	735.47
All SAFA Districts	4,164	1,052	738	2,374	$ 694.57
Percent SAFA $	100	37.0	14.3	48.6	--

* At least 50 percent of all non-Federal revenues are from State sources. Digest of Education Statistics: 1976 Edition, Table 68, NCES, Washington, D.C., 1977.

a/ Excludes districts for which no LCR was available.

b/ This column also includes some districts whose rates were determined under a special exception provision which permits the Commissioner to establish rates above those that would result from any of the three regular calculation methods. These districts must be heavily impacted and show that rates resulting from the other methods would not be sufficient for the district to provide an adequate level of education.

SOURCE: 1976 SAFA Program Data File.

Controversies Surrounding Current Methods

As has been demonstrated, the current law offers districts and State education agencies a variety of methods from which to choose when calculating their local contribution rates. Proponents of the present system argue that it is appropriate to offer this variety because more than one method of calculating costs is needed for the program to be responsive to the diversity of State and local finance arrangements that exist throughout the nation. They also note that, given the lack of any suitable direct measure of what district revenues and costs would have been in the absence of Federal activity, the present set of alternative methods constitutes a reasonable compensation arrangement.

Critics of the present compensation system look with disfavor on this "something for everyone" approach. They are especially critical of the comparable district method which they contend is applied imprecisely, is disequalizing, and subject to abuse. The minimum payment provisions have also been criticized as disequalizing because they promote windfall gains and overpayments to some districts. The following discussion examines several of these issues more closely.

The comparable district method. In applying this method a school district is instructed to compare itself with other districts or district groupings and select one that is comparable.

Comparability is determined on the basis of certain criteria which are specified in regulations. These criteria include several which are relatively unaffected by Federal activity. Examples are district legal classification, curriculum offered, and percentage of pupils transported. For the most part, however, the criteria specified are ones that can be highly influenced by the presence of Federal children. For example, it is difficult to imagine how expenditures per pupil, pupil-teacher ratios or assessed property valuation per pupil -- all of which are included in the list of criteria -- possibly could be unbiased comparative characteristics.

Indeed, one of the major dilemmas which must be confronted in applying any comparable district approach is that if a district is truly impacted by Federal activities it is not likely to have non-impacted comparables. Thus, although the comparable district method is often justified on the basis that it provides a solution to the problems associated with using an Impact Aid district's Federally influenced education costs to determine its rate of compensation, in fact, the method is at best an imperfect solution to these difficulties.

A second problem that besets the comparable district method relates not so much to the appropriateness of the criteria as to the nearly impossible task of establishing consistent rules for how they are to be applied. Even if such

rules could be devised, the task of monitoring to determine the accuracy of each district's data collection procedures and selection methods would still cause overwhelming practical difficulties. It is probably because of these problems that only the broadest standards and most flexible review procedures have been adopted by the program. However, these practices are the source of major criticism. For example, the GAO recently noted that:

> OE has not defined tolerances that applicants can use in selecting comparables which are dissimilar in several criteria or which do not otherwise meet OE requirements for comparability. Although instructions state that cost per pupil is the primary criterion for determining comparability, neither the regulations nor the instructions specify what weight should be given to the remaining criteria.1/

Consequently, there is no consistent or systematic procedure for selecting comparables or for use by OE in approving selections. Moreover, such wide latitude provides a powerful incentive for districts to maximize their Federal grant by placing greatest emphasis on those characteristics that permit them to select comparable districts that are high spenders.

The magnitude of the advantages gained by different types of districts that use the comparable district method is suggested by Table 5. The table shows the extent to which different types of districts received larger LCR's in 1976 by using the comparable district method, rather than the

1/ General Accounting Office, Assessment of the Impact Aid Program, 1976, p. 32.

Table 5. Relative Advantage of Using the Comparable District LCR Method: Ratio of Comparable District LCR's to Larger to Minimum LCR Calculations by Selected District Characteristics -- 1976[a/]

Selected District Characteristics	Ratio of Comparable District LCR to Larger of Minimum LCR's[d/]	Percent SAFA Received by Districts Using Method[d/]
All SAFA Districts.....	1.42	37.09
Percent SAFA Pupils		
75 - 100	1.81	63.13
50 - 74	1.30	23.41
25 - 49	1.35	19.16
15 - 24	1.44	34.92
10 - 14	1.41	62.02
5 - 9	1.36	26.40
Less than 5	1.35	36.65
Metropolitan Classification[b/]		
Center City.....	1.37	36.25
Suburban.....	1.45	40.54
Non-Metropolitan.....	1.47	34.83
Unclassified.....	1.62	29.70
Property Per Pupil[c/]		
Lowest 25%.....	1.29	22.14
2nd Quartile.....	1.40	18.15
3rd Quartile.....	1.43	56.66
Highest Quartile.....	1.40	58.36

a/ This is the weighted average ratio of comparable district LCR's to the larger of the two minimum LCR's. Mathematically, the ratio may be stated as:

$$R = \Sigma_{dec} \frac{\left[A_{dec}\left(\frac{C_{dec}}{M_{dec}}\right)\right]}{A_c}$$

where R = the ratio calculated
A = SAFA ADA
C = Comparable District LCR
M = Larger of 1/2 State or national average expenditures per pupil
d = District d
c = Category c (e.g., center city district, lowest wealth quartile, etc.)
s = State s
ε = "a member of" -- e.g., dεc = district "d" a member of category "c".

b/ Approximately 650 districts could not be assigned a metropolitan status classification. Most of these unclassified districts are small and therefore likely to be non-metropolitan in character.

c/ Districts assigned to quartiles based on within-State ranking of all districts. Property value is for 1974-1975. Districts without LCR's omitted from analysis.

d/ This column also includes some districts whose rates were determined under the special exception provision which permits the Commissioner to establish rates above those that would result from any of the regular calculation methods.

SOURCE: 1976 SAFA Program Data File Matched with 1970 Census and 1974-1975 Equalized Property Value Data

higher of the two minimums. For example, the table indicates that, on average, the LCR in districts using the comparable district method was 42 percent higher than it would have been had the most favorable minimum rate been used. The table also shows the percent of SAFA payments received as a result of these districts' use of the comparable district method.

As can be seen, the major beneficiaries of this calculation method were districts in the highest impact category. The LCR for these districts was, on the average, about 81 percent higher than it would have been using the most favorable minimum calculation method. In addition, about 63 percent of these districts' funds were received because they used this method to calculate their rates.

Heavily impacted districts are not the only above average beneficiaries of the comparable district method. Other types of districts, notably those in non-metropolitan and suburban areas and those with above average property wealth, also benefited.

That districts in the third and fourth (wealthiest) quartiles of property wealth received, respectively, about 57 and 58 percent of their funds using this approach and also obtained high relative compensation rates (about 40 percent more than they would have received using the minimum method), is evidence of the disequalizing properties of the comparable district method. Though many will argue that it is entirely

appropriate for high wealth districts to choose comparables that also are wealthy, others will find it difficult to justify a compensation method that results in large "bonuses" to districts which maintain their high relative property wealth status, even though the Federal government operates within their boundaries. Many others will also question whether it is appropriate for the Federal government to distribute its funds in a manner that undermines State school finance reform efforts by making these wealthy districts even wealthier.

When all is said and done, comparable district calculations are a major weak point of the present program. Their use probably should either be restricted or eliminated entirely. Later we will explore several ways of accomplishing this. For now we turn to a brief discussion of the two minimum calculation methods.

Minimum payment provisions. Districts in States where large percentages of total educational costs are defrayed by State aid contributions, or where the overall level of education support from all sources is relatively low, will generally do poorly using the comparable district method. This has been deemed politically unacceptable, and consequently the two minimum payment methods are made available to those districts that wish to use them. In general, the State average minimum has been a popular alternative in high expenditure

States, while the national average minimum has been used in States which are less wealthy than others or which provide lower overall levels of support for education.

Critics of the minimum methods have argued that their use, especially by low tax effort districts, results in unjustifiable windfall gains. These overpayments result when the minimum Federal grants received by a district yield Federal per pupil amounts that are larger than the per pupil amounts guaranteed non-Federal pupils at prevailing tax rates and State aid levels. Many observers suggest that such distributions bring discredit to the Impact Aid program and, by implication, all Federal education programs. They also note that the minimum payments discourage local tax effort and expend Federal funds where they are least needed.

The Stanford study recognized these minimums as the single source of SAFA overpayments. The Battelle analysis proposed eliminating the State average minimum (because it is disequalizing across States) and cautiously recommended that the national average minimum be retained. However, to further within-State equalization efforts, Battelle also recommended that that portion of the Federal payment which exceeded a district's normal entitlement be paid to the State rather than the district.

Although there is merit to these criticisms and recommendations, it is probably unrealistic to believe that Congress would sanction an Impact Aid program that did not have some

minimum or alternative payment scheme. Moreover, as we shall discuss later, Section 5(d)(2) which was enacted as part of the 1974 Education Amendments, provides a mechanism whereby States with acceptable equalization programs can take Impact Aid into account when making State aid payments. This provision affords some States the opportunity to counteract the dis-equalizing within-State side effects of the program. Finally, although retention of the State average minimum still poses a problem for those concerned with interstate equity, it can legitimately be noted that those districts that use this method most frequently, are located in States with heavy concentrations of special need and other high cost children to educate. Recent evidence also suggests that, in real terms, these States are less wealthy and more in need of higher compensation rates than was true in the past.

Entitlements-Weights[1/]

The final portion of this section focuses on the program's current entitlement weighting scheme. Essentially, the current

1/ This section only addresses Impact Aid entitlements and does not include an analysis of the tier system. This is because the tier system is not intended to reflect relative burdens, but simply to set priorities for payment when the program is not fully funded. It should be noted, however, that the priorities in Tier 2 generally correspond to the weights assigned in the entitlement scheme. In other words, those categories of children assigned the highest entitlements are paid the highest percentage of their entitlement in Tier 2, and children assigned the lowest entitlements are paid the lowest percentage of their entitlement in Tier 2.

weighting system is designed to adjust the local contribution rate for each of the different types of Federal children that comprise a district's enrollment. Theoretically, these adjustments are intended to reflect the fact that some children constitute greater or lesser local revenue losses for a district than others. Originally, the Impact Aid program provided entitlements at only two different rates: Entitlements for "A" children were 100 percent of the local contribution rate and those for "B" students were 50 percent. The present program, however, assigns seven different entitlement percentages for 15 categories of children. This weighting scheme was implemented by the 1974 Amendments in order to "fine-tune" the program so that it would more accurately compensate for the different types of burden associated with each type of Federally connected child.

The following discussion focuses on the question of whether the relative weights for the categories of children are reasonable reflections of the Federal burden each represents. We do not here determine whether a particular weight quantifies a precise burden. Doing that would require much more detailed and reliable fiscal data than are available now for Impact Aid school districts. We do try to examine the assumptions underlying the different entitlement percentages in order to determine whether the weights assigned are reasonable and the variations are based on valid distinctions.

The major difference in entitlements is between those for "A" children and "B" children. The "A" and "B" distinction has been a feature of the program since it began. Entitlement weights for "A" children are the highest (90 to 150 percent of LCR) to compensate for the loss of both residential and non-residential property tax revenues. In general, "B" entitlements are slightly less than one-half the "A" entitlements (40 to 75 percent of LCR) to compensate for the loss of either residential or non-residential property, but not both.

This basic difference between "A" and "B" entitlements reasonably corresponds to the relative tax losses associated with the two types of children. That is, the practice of assigning "B" children weights of about one-half those assigned their "A" category counterparts seems reasonable because "B" children constitute a loss of only half of total local education revenues (i.e., the non-residential portion), while "A" children are associated with a 100 percent loss of both place-of-work and place-of-residence related revenues.1/

Other justifiable weighting differences are those assigned for children of parents in the uniformed services

1/ See Advisory Commission on Intergovernmental Relations: Financing Schools and Property Tax Relief, January 1973, p. 25. The report indicates that total local tax revenues are about equally divided between those from residential and those from non-residential sources.

and for military and Indian handicapped children. The higher entitlement percentages for military children (100 percent for "A's" and 50 percent for "B's") reflect the additional revenue losses which are associated with military as compared with civilian personnel. These losses result from the use of base commissaries rather than local stores, and the exemption of military personnel from State or local income and personal property taxes in districts where they are stationed.

For entitlement purposes, military and Indian handicapped children are counted as one and one-half of their non-handicapped counterparts, resulting in entitlement weights of 150 percent for "A" children and 75 percent for "B" students. These special adjustments are justified in part by the higher costs of providing special education programs for handicapped children. They are also intended to provide a partial offset for districts whose special education costs have been increased by Federal policies that cause higher than average numbers of handicapped children to locate in districts where special education services are available. These policies have generally resulted in abnormally high concentrations of costly handicapped military children in districts with special education programs of above average quality.

The relative magnitude of some of these adjustments is open to question. For example, from the perspective of most special education interest groups, the weights are probably

only about three-fourths of what they ought to be in order to reflect accurately the often cited 200 percent cost differential between handicapped and non-handicapped children.

On the other hand, where the Impact Aid program is concerned, the use of this 200 percent figure may be somewhat misleading. It is based on average total excess costs for the nation as a whole, not average excess costs for local school districts. Thus, where excess costs are defrayed largely by State governments a 200 percent entitlement weight may be excessive. Moreover, the current program permits districts to take these extra costs directly into account when selecting comparable districts and calculating local contribution rates. Thus, to the extent that districts with heavy concentrations of military of Indian handicapped children are able to choose comparables with equally large concentrations of handicapped children, their LCRs should at least partially reflect the increased local share of costs associated with educating such students. Increasing these rates by 150 percent may, in fact, represent overcompensation for some of these districts.1/

It is not possible to conclude with any great certainty that the present entitlement weights for military and Indian

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1/ This argument is not perfect. That is, some predominantly military districts with inordinately large numbers of handicapped children may find it impossible to identify comparables with similar large concentrations of handicapped children. In such instances, LCR's based on average costs may understate these districts' revenue requirements.

handicapped children are precisely accurate. On the other hand, the fact that special costs may be included in the LCR calculation, and the provision for higher entitlements primarily in districts where Federal policies may result in higher than average numbers of handicapped children and where districts are actively providing special services, all seem to be defensible practices. Although the higher weights for handicapped military and Indian children may not be precisely accurate, they do seem to be based on appropriate and valid distinctions.

Some features of the entitlement weighting scheme are not as justifiable as those discussed to this point. In particular, it is not entirely clear why civilian "A" children in lightly impacted districts (i.e., those with less than 25 percent of their enrollments comprised of "A" children) are paid at lower rates than their peers in high impact districts (90 percent compared to 100 percent). No similar distinction is made within the "B" category. Although a strong case can be made that low impact districts are less burdened by Federal activities and should be given lower priority in the program, it can be argued that the weighting scheme is not the appropriate place to address this issue. Since entitlement weights are based on characteristics associated with particular types of children, it is somewhat inconsistent to use the characteristics of a district, as opposed to a student, as the basis for providing different entitlements. District characteristics would seem

to be more relevant to the calculation of local contribution rates or to determinations of district eligibility to receive Impact Aid payments, and therefore have been addressed in the sections which cover these features of the program.

From the foregoing analysis we would conclude that, for the most part, the entitlement weighting scheme is reasonably well designed to compensate for the revenue and educational burdens associated with the various types of Federally connected children. While it is not possible, using available data, to measure precisely the burdens and assign accurate weights, the assumptions underlying the weights are valid and reflect a greater sensitivity to the relative burdens imposed by different types of children than did pre-reform entitlements. It could also be contended that the current law provides the maximum degree of "fine-tuning" that is warranted at this time.

This assessment has focused on the burdens arising from the characteristics of eligible children. The following section examines the characteristics of Impact Aid districts and assesses whether Impact Aid funds are distributed equitably in terms of district needs and Federal impact.

Are Impact Aid Funds Equitably Distributed in Terms of District Needs and Federal Impact?

A longstanding criticism of the Impact Aid program is that is distributes large amounts of money to affluent districts--

districts that could easily support a high level of educational expenditure without Federal assistance. A related criticism concerns the appropriateness and wisdom of distributing scarce Federal dollars to lightly impacted districts. The following discussion will explore both of these issues.

Impact Aid and District Wealth[1/]

Many have argued that the Impact Aid program is inequitable because it distributes funds to affluent districts that could easily support a high level of educational expenditures without Federal assistance. Indeed, critics have contended that some districts are wealthy, in part, because they are benefited, not burdened, by Federal activities. Others merely observe that eliminating or reducing these payments would hardly be felt by wealthy districts because Impact Aid amounts per pupil are small and could easily be absorbed locally through modest tax increases. These persons note that eliminating or reducing such aid would free-up a substantial portion of the total SAFA appropriation for use by less wealthy districts. Alternatively,

1/ Throughout this analysis "affluent" and "wealthy" are used synonymously with property wealth per pupil above the State average. Although parallel analyses were conducted using various measures of income wealth, the property wealth measure was deemed more appropriate in the context of the Impact Aid program.

these monies could be spent for other more important educational purposes.

Evidence bearing on the validity of these criticisms is provided below in Table 6. The table shows that in 1976 there was some substance to these allegations for, although the distribution of total SAFA payments per pupil was somewhat progressive across districts classified by property wealth, a significant share of aggregate program dollars went to a large number of districts which, in their own States, would have been considered relatively well-off. Thus, even though the poorest districts received about twice what the least poor districts received in total SAFA dollars per pupil, about 20 percent of all SAFA dollars went to high property wealth districts.1/

Closer inspection of Table 6 shows that there are major differences between the way "A" and "B" category payments affect total funding in wealthy and poor districts. Specifically, although both types of payments tend to be inversely distributed across districts ranked by property wealth, most wealthy districts receive the bulk of their funds for "B" category children while poor districts receive their funds because they have large concentrations of high burden "A" category children.

1/ A similar but more pronounced pattern emerges for districts ranked by median family income. Fully 42 percent of all SAFA monies accounted for by our sample were targeted on districts in the highest quartile of median family income.

Table 6. Payments to SAFA Districts Classified by Property Wealth -- 1976 (Through Tier 2)[a/]

Property Per Pupil (ADA) [c/d/e/]	Total SAFA/ Pupil[b/c/] (1)	SAFA "A"/ Pupil[c/] (2)	SAFA "B"/ Pupil[c/] (3)	% SAFA Dollars[c/] (4)	SAFA $ Millions[c/] (5)	# of Districts (6)
National Average (Total).....	$ 23.96	$ 8.06	$ 12.83	100.00	$ 519.2	3,374
	....(U.S. Average=1.00).....					
Poorest.....	1.6	2.4	1.2	36.9	$ 191.4	999
Quartile 2.....	0.9	0.8	1.0	24.8	128.7	880
Quartile 3.....	0.9	0.6	0.9	19.1	99.4	770
Least Poor.....	0.7	0.4	0.8	19.2	99.8	725

a/ Not included in FY 1976 SAFA payments are amounts distributed under Section 2: money paid to other Federal agencies under Section 6; amounts paid out for major and pinpoint disaster assistance under Section 7; and any payments made at Tier 3 levels. Total SAFA includes hold harmless amounts. These amounts are excluded from SAFA "A" and "B" totals.

b/ SAFA per pupil amounts on this and subsequent tables are calculated based on total ADA rather than only Federal ADA. Total ADA was used because most Impact Aid is general assistance and is used for all students.

c/ Details for property wealth will not add to U.S. totals because these distributions are based on different subsets of SAFA districts. Subsets consist of those districts on the SAFA program data file which could be matched with districts on other files containing property data. Note that percentage distributions in Column (4) are based on SAFA dollars distributed to the matched districts.

d/ Districts are assigned to quartiles based on their within-State rankings. SAFA districts are ranked with non-SAFA districts in this process.

e/ SAFA data are for 1976. Property data are for 1974-1975.

SOURCE: 1976 SAFA Program Data File Matched with 1974-1975 Equalized Property Value Data.

These data substantiate claims that large amounts of Impact Aid are targeted on the wealthy, but do not indicate whether wealthy districts could absorb the loss of these payments through relatively modest increases in tax and other revenues. Information bearing on this claim is provided in Table 7 which shows how much local (and also State plus local) revenues would have to be raised by districts in different wealth quartiles in order for them to fully offset a total loss in their Impact Aid payments. The table shows that, in the aggregate, districts in the highest quartile of property wealth could offset such losses by increasing local revenues by about 1.7 percent. State plus local revenues would have to be raised by only 1 percent.

Table 7. SAFA Payments to Districts Classified by Property Wealth: SAFA as a Percent of Local and State Plus Local Revenues -- 1976 (SAFA Through Tier 2)

Property Wealth Per Pupil (ADA)	Number of Districts in Sample (1)	SAFA $ As a Percent of Local Revenues (2)	SAFA $ As a Percent of State + Local Revenues (3)
Total.....	2,039	2.9	1.6
Poorest.....	588	6.1	2.8
Quartile 2.....	537	3.0	1.6
Quartile 3.....	472	2.4	1.5
Least Poor.....	442	1.7	1.0

SOURCE: 1976 SAFA Program Data File Matched With 1974-1975 ELSEGIS and 1974-1975 Equalized Property Data.

Although these aggregate data do not indicate the effects of aid reductions for individual districts, they do provide at least partial evidence to support the complaints of Impact Aid critics. Substantial amounts of money are being channeled to wealthy districts in relatively small per pupil amounts -- amounts which apparently could be reduced or eliminated without causing much difficulty for the districts involved. It is also clear that many of these funds result from entitlements for the least burdensome "B" children, while the most needy districts receive their Impact Aid assistance because they are truly burdened by large proportions of "A" children.

It would be tempting to use these data to support the argument that wealthy districts are being unfairly overcompensated by the program. Given the limited resources that are available, one could conclude that it makes little sense to continue payments that make wealthy districts wealthier. On the other hand, many wealthy districts could argue quite forcefully that it is inappropriate to consider their relatively favorable economic positions in compensating for Federal impact. They might contend, for example, that they would be even wealthier without the presence of the Federal government and that it is unfair for the Federal sector to create even the smallest burden without providing offsetting compensation. Own view lies somewhere in-between -- wealthy districts may be correct when they argue that it is unfair to discriminate

against them because they are wealthy, but are on less firm ground when they argue that the Federal government has a responsibility to compensate for even the smallest burden.

Impact Aid and Federal Burden

A related criticism of the program concerns the fact that a significant fraction of all Impact Aid districts are lightly impacted, containing fewer than 10 percent Federally connected children. For example, Table 8 shows that in 1976, 60 percent of all Impact Aid districts were lightly impacted by this definition. The table also shows that even though these lightly impacted districts received very small per pupil grants (grants that averaged about $13 or less per pupil) in the aggregate they accounted for a substantial 20 percent of all Impact Aid dollars (about $122 million). As can be seen, most of these funds were received for "B" category children. In contrast, most of the funds received by heavily impacted districts resulted because of their disproportionately large share of high burden "A" children.

As we have noted, many would argue that these payments to lightly impacted districts are entirely appropriate. They would note that degree of impact has nothing to do with the Federal government's moral responsibility to compensate for the burden it causes. They would suggest that any attempt to reform the present program by reducing or eliminating these payments would be improper because it would constitute

Table 8. Payments to SAFA Districts by Percent SAFA Children -- 1976 (Through Tier 2) a/

District Characteristic	Total SAFA/ Pupil (1)	SAFA "A"/ Pupil (2)	SAFA "B"/ Pupil (3)	% SAFA Dollars (4)	SAFA $ (Millions) (5)	# of Districts (6)
National Average (Total)	$ 26.39	$ 10.35	$ 12.92	100.0	$ 610.7	4,221
	.....U.S. Average=(1.00)...					
Percent SAFA Children						
75 - 100	27.7	67.3	2.0	12.6	$ 76.8	99
50 - 74	9.5	17.8	3.9	9.0	55.0	108
25 - 49	3.5	4.0	3.2	24.3	148.6	407
15 - 24	1.7	1.1	2.0	18.3	111.7	480
10 - 14	0.9	0.4	1.3	15.9	96.9	567
5 - 9	0.5	0.2	0.7	11.8	69.0	1,247
Less than 5	0.2	0.05	0.3	8.6	52.6	1,313

a/ Not included in FY 1976 SAFA payments are amounts distributed under Section 2; money paid to other Federal agencies under Section 6; amounts paid out for major and pinpoint disaster assistance under Section 7; and any payments made at Tier 3 levels. Total SAFA includes hold harmless amounts. These amounts are excluded from SAFA "A" and "B" totals.

SOURCE: 1976 SAFA Program Data File

an abdication of the government's responsibility to pay a share of the cost of educating all Federal children.

Others may well find this line of argument difficult to accept. Given that priorities must be set on Federal resource expenditures, they will question whether it is sensible or wise for an Impact Aid program to compensate districts that are not very heavily impacted. They will note that distributing money in such small per pupil amounts to districts that are so lightly impacted diverts support away from districts that have a more legitimate claim on the program.

We think these latter arguments have particular merit. Lightly impacted districts should represent a relatively low Federal priority. The case for this position is compelling, especially when one considers the consistent pattern of differences between high and low impact districts.

For example, Table 9 compares Impact Aid payments to local (and State plus local) revenues in districts classified by percent Federal enrollment. The table shows that Impact Aid payments to districts with low percentages of Federal children are small when compared with other revenues. Thus, in districts where Federal children constitute less than five percent of total enrollment, complete elimination of Impact Aid would require offsetting increases in local revenues of about one-half of one percent. By comparison, eliminating Impact Aid payments in the most heavily impacted category of

districts would require offsetting local revenue increases of over 150 percent. Clearly, these data indicate that lightly impacted districts are much less dependent on Impact Aid funds than heavily impacted ones, and could adjust to the elimination or reduction of these payments without suffering any undue hardships.

Table 9. SAFA Payments to Districts Classified by Percent Federal Children: SAFA as a Percent of Local and State Plus Local Revenues -- 1976 (through Tier 2)

Percent SAFA Children (ADA)	Number of Districts in Sample (1)	SAFA $ as a Percent of Local Revenues (2)	SAFA $ as a Percent of State + Local Revenues (3)
Total	2,174	3.1	1.7
75 - 100	20	153.8	56.3
50 - 74	37	61.7	23.3
25 - 49	186	19.8	7.9
15 - 24	203	5.9	3.1
10 - 14	263	3.1	1.6
5 - 9	639	1.5	0.9
Less Than 5	826	0.7	0.4

SOURCE: 1976 SAFA Program Data File Matched with 1974-1975 ELSEGIS Data.

Finally, Table 10 provides additional information about the needs of different types of Impact Aid districts. The table shows property wealth for districts in each impact category relative to these districts' State averages. For example, the table indicates that districts in the highest impact category have only about 55 percent of the average property wealth for all districts in their respective States. A quick perusal of the information presented indicates that Impact Aid districts have about average wealth overall, but that heavily impacted districts show real evidence of burden from loss of property due to Federal activity. On the other hand, lightly impacted districts are generally at or above average in terms of property wealth. Once more, lightly impacted districts do not seem to have been very heavily burdened as a result of Federal activity. Given these data, one might reasonably conclude that, if Federal funding priorities must be set, heavily impacted districts whose burdens are relatively unambiguous, are much more deserving of compensation than lightly impacted ones whose burdens are less apparent.

Does the Program Interfere With State Equalization Programs?

A major criticism of the Impact Aid formula has been that it allocates assistance to districts in ways that disregard and undermine State equalization programs. Originally,

Table 10. Property Per Pupil for SAFA Districts by Percent SAFA Children Shown Relative to State Average for All Districts[a/]

% SAFA Children (ADA)	Number of SAFA Districts in Sample[b/] (1)	Equalized Property Value Per Pupil (ADA) Relative to State Averages[c/] (2)
All SAFA Districts	3,374	0.99
75 - 100	38	0.54
50 - 74	60	0.56
25 - 49	257	0.72
15 - 24	342	0.95
10 - 14	433	1.10
5 - 9	1,034	0.99
Less than 5	1,201	1.00

a/ Districts are assigned to impact categories based on FY 1976 Percent SAFA Average Daily Attendance. Property value data are for 1974-1975.

b/ Sample is comprised of all FY 1976 SAFA districts in the SAFA 1976 program data file which could be matched with the 1974-1975 property value.

c/ For districts in each degree of impact category a weighted average was calculated for the ratio of property per pupil in each district to the average property per pupil in the district's particular State. The values in Column (2) indicate how much more or less, on average, district property per pupil was than State average property per pupil for the aggregate of districts in a particular degree of impact category. Mathmetically, this average ratio may be written as:

$$I = \frac{\Sigma_{d\varepsilon c}\left[A_{d\varepsilon c\varepsilon s}\left(\frac{E_{d\varepsilon c\varepsilon s}}{E_s}\right)\right]}{A_C}$$

where I = the index shown in Column (2)
A = ADA
E = Property per pupil
d = District d
c = Category of impact c
s = State s
ε = "a member of" -- e.g., $d\varepsilon c$ = district "d" a member of category "c".

SOURCE: 1976 SAFA Program Data File Matched with 1974-1975 Equalized Property Value Data

the Impact Aid statute was silent on the issue of whether States could take Impact Aid payments into account in determining State assistance to Federally impacted districts. As as result, a number of States added provisions to their school finance laws that permitted them to substitute Impact Aid money for their own assistance to school districts. Many justified these added provisions by noting that they facilitated the use of Impact Aid funds in a manner consistent with State policies to equalize the ability of school districts to finance education. In effect, these States argued that these Federal monies were part of a school district's resources and that taking them into account for the purpose of determining a district's share in the State aid program was therefore appropriate and proper.

In 1968 a provision (Section 5(d)(1) of the current law) was added to P.L. 81-874 which would have terminated payments in any State that took Impact Aid into account when determining a district's eligibility for or share in a State aid program. Behind this prohibition was the notion that Impact Aid is provided to offset the loss of local revenues from Federal activities, not to supplement State aid programs. Proponents of the prohibition argued that localities receiving Impact Aid should not be penalized for their participation in the program by having State aid reduced.

Although the prohibition stood more-or-less intact for several years, valid complaints from States that were enacting reforms of their school finance systems forced a change in the rules governing its application. Specifically, the 1974 Amendments added an exception to the prohibition for States which have enacted school finance laws "designed to equalize expenditures." The exception recognizes that where expenditures are being equalized by a State program, Impact Aid can result in "windfalls" to districts and thus prevent the State program from equalizing. Furthermore, when a State has a fully equalized program, it is most likely bearing some of the burden resulting from Federal activities, and the exception appropriately permits States to realize some relief from Impact Aid.

The law also contains a proviso designed to limit the extent of substitution in districts where total local revenues exceed the amount covered under the State equalization plan. Thus, if one quarter of local revenues are in excess of the amount covered by the State plan, then one-quarter of the Impact Aid payments to that district cannot be counted in calculating the State's contribution.

A brief example will illustrate how this limitation proviso operates in a State with a "foundation" plan for State aid which guarantees school districts a specified amount per pupil if a minimum tax effort is exercised. In a State where the foundation plan guarantees $1,000 per pupil, and

the district is able to raise $600 by taxing at the prescribed rate, the State will provide the remaining $400 needed to reach the foundation amount of $1,000. If the district taxes itself at a higher rate and thereby raises an additional $200, this amount will supplement the foundation and not be counted in calculating the State payment which will still be $400. Thus, as a result of its extra effort, the district will have available $1,200 per pupil. If the district also receives $100 per pupil for Impact Aid payments, the proviso in the law limits the amount the State can substitute to three-fourths of the Impact Aid payment: that is, the ratio of local revenues covered under the State equalization plan ($600) to total locally raised revenues ($800.). Thus, the State can reduce its payment to the district by $75, to $325, but cannot substitute the full $100 of Impact Aid. As a result, the district will have $1,225 per pupil, after the Impact Aid payment.

As can be seen from this example, the provisio has the effect of treating Impact Aid payments as if they were locally raised revenues, part of which would be raised at the prescribed tax rate and counted toward the foundation amount ($75 out of $100), and part of which would be raised from the additional effort and considered supplemental ($25 out of $100). Since Impact Aid is primarily intended to replace lost local revenues, this treatment is appropriate. It prevents Impact Aid districts from being given an advantage over non-Impact Aid districts merely because their payments are from the Federal government

rather than locally raised revenues. That is to say, the proviso prevents Impact Aid districts from receiving "windfall" payments.

Moreover, by limiting the amount of Impact Aid the State can substitute for State Aid, the proviso also assures that districts will not be "penalized" as would be the case if the State could substitute the full amount. The penalty would be that districts would receive no additional funds from Impact Aid, even though if the funds had been locally raised, the district would have realized some supplemental funds. Consequently, it can be said that the proviso is neutral with respect to the State's equalization plan, neither providing disequalizing windfall payments to districts nor permitting excessive substitutions of Impact Aid for State Aid. In effect, it allows the State plan to equalize the revenues that can be raised with a given tax effort for all districts in the State.

In order to qualify for the exception and be permitted to substitute Impact Aid for its own aid, it must first be determined that the State has an equalization plan. The law's general qualifying test defines an equalization plan as a shared cost program which takes local wealth into account and which has not been found to be unlawful by the State court. Over 45 States are estimated to have State Aid plans which meet this description.

In addition to this general test, the exception provision has required the issuance of regulations establishing operational tests for determining whether a State has an "adequate" equalization program. Two alternative tests have been developed to assess the extent to which State aid formulas are equalized.[1/] The first is the so-called "disparity" test. Under this test, a State is considered adequately equalized if there is a disparity of no more than 25 percent between per pupil expenditures for the fifth and 95th percentile of students. This test is very restrictive, with perhaps only four States expected to qualify. The disparity test has been criticized as being too inflexible to allow for the higher costs of educational resources in cities or to accommodate legitimate variations in school finance reform efforts. For example, States using "district power equalization" formulas, which take into account the relative taxing effort of districts, may well be excluded by a disparity test.

As a result of these criticisms an alternative "wealth neutrality" test was devised which measures the degree to

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1/ The regulations also provide for a special exemption if the Commissioner determines that the tests should not be applied due to exceptional circumstances within the State. To be considered for the special exemption, the amount of education revenues available to districts under the State plan must not be predominately a function of district wealth; the program must be designed to provide financially adequate education programs and supportive services for all public school pupils in the State, and the counting of Impact Aid must result in more equalized expenditures or revenues for education within the State.

which a State's program assures that the same local tax effort will produce an equal educational yield. This test reflects the view that substantial expenditure differences resulting from above average student needs and educational costs may be necessary to provide equal educational opportunity. Differences in a school district's taxable wealth, however, should not be allowed to result in significant expenditure disparities.

A State will qualify under the neutrality test if 85 percent of its educational revenues are raised in a "wealth neutral" way -- that is, financed from the wealth of the State as a whole rather than from a local tax base. Revenues are considered wealth neutral if they are generated by a program which guarantees all districts within the State equal revenue per pupil for equal tax effort, or if they are distributed by the State on the basis of some objective measure of pupil need. It is expected that this test will prove as strict and narrow an exception as the disparity test.

Because these tests are so restrictive, it is argued that they provide only a partial solution to coordination with State equalization aid. This is especially the case for those States which do not qualify (i.e., most States), since Impact Aid funds actually impede their ability to reduce disparities. As shown in Table 11 (column 1), although most Impact Aid districts in our sample rank in the lowest two quartiles of State and local revenues per pupil within their States (1,162 districts), a

TABLE 11 Effects of SAFA Revenues Per Pupil on SAFA Districts Classified by State Plus Local Revenues Per Pupil — 1976 (SAFA Through Tier 2)

State + Local Revenues Per Pupil (ADA) a/	Number of SAFA Districts in Sample	% SAFA $ to Districts in Sample	Average Index of: b/ Non-Fed'l Rev./ADA Rel. to St. Avg. Non-Fed'l Revenue	SAFA Rev. /ADA Rel. to State Average Non-Fed'l Revenue	SAFA+Non-Fed'l Rev./ADA Rel. to St.Average Non-Federal Revenue +SAFA
	(1)	(2)	(3)	(4)	(5)
Average All SAFA Districts (Total)	2,174	100.0	1.010	0.018	1.015
Lowest.....	602	39.4	0.876	0.025	0.890
Quartile 2....	560	21.1	0.953	0.016	0.957
Quartile 3....	499	17.2	1.050	0.013	1.050
Highest.....	513	22.4	1.193	0.018	1.194

SOURCE: 1974-1975 ELSEGIS — 1976 SAFA Matched File.

a/ SAFA districts are ranked and classified in combination with non-SAFA districts and assigned to quartiles based on within-State rankings.

b/ Indices are calculated as follows:

$$I = \frac{\Sigma_{d \varepsilon q} \; A_{d \varepsilon q \varepsilon s} \left(\frac{R_{d \varepsilon q \varepsilon s}}{R_s} \right)}{A_q}$$

where: A = ADA

R = Revenues per pupil (either non-Federal, or Non-Federal plus SAFA), as appropriate.

d = District d

q = Quartile q

s = State s

ε = "a member of" -- e.g., $A_{d \varepsilon q \varepsilon s}$ equals ADA in district d, a member of quartile q in State s.

significant number of districts appear in the top two quartiles (1,012 districts), and thus would have relatively high resource levels even without Impact Aid funds. These districts receive about 40 percent of the total Impact Aid funds which are accounted for by our sample of districts.

In addition, column 5 suggests that while, for the most part, Impact Aid has an equalizing effect, this effect is, at best, very slight. Thus, the net effect of SAFA payments is only a small reduction in the disparity of per pupil revenues between the top and bottom revenue quartiles -- from 1.362 (1.193:0.876) to 1.342 (1.194:0.890).

When all is said and done, perhaps the major criticism of Impact Aid from the standpoint of equalization relates not so much to what it does, but what it fails to do. It fails to give some States an incentive to reform their finances. It fails to give States that have made a modest start toward equalization an opportunity to achieve further gains by off-setting payments to relatively well-to-do districts. As previously noted, about 40 percent of SAFA dollars go to districts in the top two revenue quartiles, and the effect of these payments is often to increase the distance between spending levels in these districts and the State average. Table 12 illustrates this point for nine districts in three States. In two of these districts, SAFA payments more than double the district's advantage relative to State averages.

Table 12. Effect of Impact Aid Payments on Expenditures Per Pupil of Selected High Impact Districts in the Top Decile of Their States on Non-SAFA Spending: 1974 - 1975

Selected Districts (by States)	Total Pupils	Ratio of Expenditures Per Pupil to State Averages (shown in parens)		
		Non-SAFA	SAFA	Total
New Mexico	362,250	($726)	($39)	($765)
Los Lunas	4,503	1.39	9.44	1.80
Central	6,160	1.30	7.41	1.61
Las Vegas	3,614	1.15	4.64	1.33
North Dakota	133,278	($930)	($18)	($948)
Mandaree	154	1.87	33.00	2.46
White Shield	165	1.48	22.83	1.89
Solen	360	1.15	18.33	1.48
Virginia	1,091,095	($916)	($15)	($931)
Falls Church	1,643	1.97	9.67	2.09
Fairfax City	5,064	1.44	5.20	1.50
Fairfax County	137,154	1.35	7.47	1.45

SOURCE: National Council of State Legislators, Impact Aid and Basic School Finance Programs: Can They be Made More Compatible?, 1976. (Special tabulation.)

Our discussion and analysis suggest that substantial benefits for State financing of education can be achieved through further Impact Aid reforms which relax present standards of equalization to permit more state offsetting of payments received by high resource districts. Section III will explore these reform options in greater detail.

The Present Program In Perspective

The preceding evaluation suggests that by FY 1976 the Impact Aid reforms of 1974 were only partially successful in addressing most "pre-reform" criticisms of the program. For example, while entitlements for several questionable types of children were eliminated or reduced, new provisions were added that guaranteed funding for other, equally questionable categories. Similarly, although important first steps were taken to reduce the disequalizing effects of the program by allowing States with "adequate" equalization systems to waive the restriction against taking Impact Aid payments into account when making State aid allocations, strict qualifying tests will prevent most States from taking advantage of the waiver. Finally, as we have shown, substantial FY 1976 Impact Aid payments continued to flow to districts that were not very burdened by Federal activity -- districts that many would argue have only a low priority claim on Federal Impact Aid dollars.

This is not to say that the 1974 Amendments accomplished nothing. Indeed, Table 13 indicates that some major distributional changes did occur between FY 1975 and FY 1976. The table compares SAFA payments to districts grouped according to their percentage of Federal children for 1975, the year before reform and 1976, the year in which the reform was partially implemented for the first time.

As may be seen (Column 4), reform seems to have reduced the percentage share of total SAFA dollars received by districts in the two lowest categories of impact. Overall, these two groupings' share of the total SAFA budget was reduced by about four percentage points, dropping from 24 percent in 1975 to about 20 percent in 1976.

Interestingly, the combined share received by districts in the three most heavily impacted categories also declined somewhat from 1975 levels. Although districts in the two most heavily impacted categories experienced minor share increases, reductions to districts in the 25-49 percent grouping more than offset these gains. Thus, the combined share of total SAFA dollars to heavily impacted districts declined by about five percentage points -- from about one-half of total funding in 1975 to about 45 percent in 1976.

The table shows that districts in the moderately impacted categories (i.e., those with Federal enrollments of between 10-24 percent) achieved major share increases in 1976. The

Table 13. SAFA Payments to Districts by Percent SAFA Children -- 1975, 1976 Tier 2 and 1976 Full Reform[a]

Percent SAFA Children	Total SAFA $/ADA (1)	SAFA "A" $/ADA (2)	SAFA "B" $/ADA (3)	% SAFA Dollars (4)	Total SAFA $ (Millions) (5)	Number of Districts (6)	Total ADA (Thousands) (7)
1975 Payments[b]							
U.S. Average (Total)	$ 23.58	$ 8.96	$ 14.63	100.0	$ 542.5	4,215	23,003.3
75 - 100%	$ 629.37	$ 587.92	$ 41.45	12.3	$ 66.8	106	106.1
50 - 74%	230.51	166.98	63.53	8.8	47.9	104	207.7
25 - 49%	91.14	30.99	60.15	29.4	159.2	418	1,747.2
15 - 24%	52.19	17.22	34.96	17.4	94.2	434	1,804.1
10 - 14%	28.38	5.90	22.49	7.9	42.8	493	1,506.1
5 - 9%	15.65	2.10	13.55	11.6	62.9	1,095	4,022.2
< 5%	5.05	.47	4.58	12.7	68.8	1,565	13,609.8
1976 Tier 2 Payments[c]							
U.S. Average (Total)	$ 26.39	$ 10.35	$ 12.92	100.0	$ 610.7	4,221	23,138.4
75 - 100%	$ 731.86	$ 695.85	$ 25.45	12.6	$ 76.8	99	105.0
50 - 74%	250.60	183.83	50.61	9.0	55.0	108	219.6
25 - 49%	91.21	41.02	40.66	24.3	148.6	407	1,629.2
15 - 24%	43.55	11.65	25.61	18.3	111.7	480	2,563.6
10 - 14%	24.80	4.09	16.38	15.9	97.0	567	3,910.5
5 - 9%	12.27	1.57	8.99	11.3	69.0	1,247	5,623.5
< 5%	5.78	.50	4.27	8.6	52.6	1,313	9,087.0
1976 Full Reform[d]							
U.S. Average (Total)	$ 23.50	$ 10.97	$ 12.52	100.0	$ 512.3	3,876	21,806.5
75 - 100%	$ 721.27	$ 695.85	$ 25.42	14.8	$ 75.7	99	105.0
50 - 74%	234.41	183.83	50.58	10.0	51.5	108	219.6
25 - 49%	81.67	41.05	40.63	26.0	133.0	406	1,627.8
15 - 24%	37.16	11.65	25.51	18.6	95.3	480	2,563.6
10 - 14%	20.31	4.09	16.22	15.5	79.3	565	3,903.0
5 - 9%	8.76	1.57	7.19	9.6	49.3	1,245	5,623.2
< 5%	3.65	0.56	3.09	5.5	28.4	973	7,764.2

a/ Not included in SAFA payments are amounts distributed under Section 2; money paid to other Federal agencies under Section 6; amounts paid out for major and pinpoint disaster assistance under Section 7.

b/ FY 1975 data include "A" and "B" plus hold harmless amount only. Districts were omitted if none of these payments were made.

c/ FY 1976 Tier 2 data include "A" and "B" plus hold harmless payments only. Purtell districts are included. Districts with no "A", "B" or hold harmless amounts have been omitted. Districts analyzed were re-classified by degree of impact where loss of eligibility for out-of-state "B" children necessitated this adjustment.

d/ FY 1976 full reform data include "A" and "B" payments only. Districts which had no such payments were omitted as were those which, due to out-of-State reforms, lost their eligibility. Purtell districts currently being phased out of the program were also eliminated because they will be ineligible when reform is fully implemented.

SOURCE: SAFA Program DATA Tapes, 1975-1976.

combined share to districts in this grouping rose by about nine percentage points -- from 25.3 percent in 1975 to 34.2 percent in 1976. Most of this increase resulted from a doubling of the shares received by the 10-14 percent category.

Most of these changes can be explained in terms of the reforms that were enacted. For example, it would appear that the reduced FY 1976 payments for many "B" category children, especially those for "B-out-of-county" and "B-out-of-State" students, were at least partially responsible for the smaller shares received by both heavily and lightly impacted districts. The reduced number of relatively heavily impacted districts (i.e., those with over 24 percent Federal enrollment) probably occurred because some had their children reclassified as "non-Federal" when out-of-State "B" entitlements were eliminated from the program. Apparently, the sorting and sifting which accompanied reform resulted in the reassignment in 1976 of a number of these districts to lower impact categories.

Reductions in payment shares and in the number of districts in the lowest category of impact can also be attributed to the sorting and sifting that accompanied these "B" category reforms. On the one hand, the category seems to have lost many districts through reclassification. That is, it is likely that many of these districts "migrated" to higher impact categories when they claimed previously uncounted public housing children toward their total Federal enrollments.

On the other hand, districts remaining in the category appear to have received lower "reform" payments for their "B" category children.

As may be seen, the moderately impacted categories experienced increases in their shares of total SAFA dollars. Not surprisingly, the shifting about which accompanied partial reform seems also to have resulted in large increases in these groupings' districts and pupils. Similarly, large district and pupil increases may be observed for the low impact 5-9 percent category. Although this grouping did not increase its share of SAFA dollars, along with the more moderately impacted categories, it seems to have been the recipient of many reclassified districts.

The 1974 reforms had important consequences for the total per pupil amounts received by different categories of districts, and also for per pupil amounts distributed for "A" and "B" category children (Columns 1-3). For example, although districts in the three most heavily impacted groupings had their combined share of total SAFA dollars reduced between 1975 and 1976, the combined per pupil amount they received increased by about $10 per child (i.e., from $132.90 in 1975 to $143.52 in 1976). Most of this increase can be attributed to normal growth in "A" category payments, although districts in these categories also seem to have received some hold harmless amounts to offset their uniformly lower "B" payments.

Districts in lower impact categories generally experienced quite different changes in their per pupil rates. The exception here is the most lightly impacted category, which seems to have experienced a slight growth in its total per pupil amount because it lost children at a greater rate than it lost dollars. Other moderate to low impact groupings seem to have had their absolute Impact Aid dollar increases diluted by even larger pupil increases. These changes resulted in lower per pupil payments for districts in the moderate to low impact range.

To the extent that the 1974 Amendments sought to reduce per pupil payments for lightly and moderately impacted districts and increase these amounts for heavily impacted ones, they seem to have been somewhat successful. As the table shows, similar successes were achieved in reducing per pupil payments for the least burdensome "B" category children and increasing payments for heavy burden "A" category students.

Table 13 also supplies information about how the program would have looked in FY 1976 had all hold harmless provisions been eliminated and had the absorption component enacted by the 1974 reforms been operating. "Purtell" districts are gradually being phased out of the program because they have lost Federal children and failed eligibility for reasons unrelated to reform. They have also been omitted from the analysis. Because Purtell districts will not be eligible

to participate in the program in subsequent years and since the law calls for phasing out the hold harmless provisions (they) expire by FY 1979) and phasing in the absorption (by FY 1978), these data provide a look at how the program would appear if it were "fully reformed" in accordance with Congressional intent. Many would argue that this is the only way to assess the 1974 reforms and not understate their effects.[1/]

The table shows that, indeed, to the extent that this is the most appropriate perspective from which to view the current program, our earlier assessment understates the changes Congress brought about. Had the program been fully reformed and funded through Tier 2, total "A" and "B" payments would have been reduced by about $30 million between 1975 and 1976 and would have totaled about $512 million. The number of participating districts also would have declined -- from 4,215 in 1975 to about 3,876 in FY 1976 -- with the majority of these losses occurring to districts in the lowest category of impact. As may be seen, districts in this category would have also experienced substantial reductions in their shares

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1/ On the other hand, some would argue that by looking at Tier 2 funding, this analysis overstates the changes resulting from reforms, since some Tier 3 payments were made in FY 1976. However, Tier 2 funding was used on the theory that it reflects Congressional intent in FY 1976, when the appropriations level was set at an amount estimated necessary to fund Tier 2, and is also comparable to subsequent appropriations which specifically limit funding to Tier 2. Inclusion of Tier 3 payments would reduce the distributional improvements achieved through Tier 2.

of Impact Aid (their share of the total would have dropped from about 12.7 to 5.5 percent) and would have lost over half of their total 1975 payments to reform.

On the other hand, heavily and moderately impacted districts would generally have increased their shares of the $512 million SAFA budget. For example, districts in the first and second highest impact categories would have received share increases of about 20 and 14 percent respectively. Once more, moderately impacted districts would have been the major beneficiaries of reform, presumably for the same reasons noted earlier.

Comparison of per pupil rates in 1975 with those that would have resulted had the program been fully reformed in FY 1976, shows that rates would have risen for the two most heavily impacted categories, but would have declined for all others. The table also shows that while there would have been a substantial 14.0 percent reduction in total "B" category payments between 1975 and 1976 under full reform, total "A" rates would have risen by 23 percent, enough to offset "B" category losses and keep total per pupil payment rates at about 1975 levels.

These comparisons and those presented earlier suggest that the 1974 Amendments made significant first steps toward addressing the Impact Aid program's major weaknesses. Nevertheless, as we have noted earlier in this section, many

questionable provisions and practices remain. Moreover, the program continues to distribute about 20 percent of its funds in relatively small per pupil amounts to over 2,500 lightly impacted districts -- districts whose Federally imposed burdens are questionable. Although in this respect the program improves upon its pre-reform predecessor, many would note that even under full reform over 2,200 lightly impacted districts would continue to receive about 15 percent of all Impact Aid dollars -- dollars that could be put to better use.

The next section will examine ways in which the precedents established in 1974 can be built upon to solve some of the program's remaining weaknesses.

III. OPTIONAL REFORM COMPONENTS

The evaluation of the current program contained in Section III suggests that there are several aspects of the program which might benefit from change. This section sets out a broad range of possible reform options which addresses the issues of burden, equity, and State equalization. Several options for change are presented which address program inequities resulting from entitlement and payment rate calculation practices. Also included are modifications designed to improve the program's ability to target on districts which are most needy because they are most heavily impacted. Still other changes are proposed which are directed toward improving coordination of Impact Aid funding and State equalization efforts. A crosscutting goal applicable to all of the options is that of achieving administrative simplification.

Presentation of the reform options includes analyses of their objectives as well as the effects each would have on program cost, district participation, and the distribution of program funds.[1/] This section is intended simply to outline and describe

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1/The analysis undertaken in this section examines changes in SAFA "A" and "B" amounts only. When changes resulting from reform components are compared with pre-reform amounts, they are based only on those FY 1976 monies districts would have received for "A" and "B" children (exclusive of hold harmless amounts and payments from other special provisions) had the FY 1974 reforms been in full effect and the program funded through Tier 2. Since reforms have been limited to changes affecting only "A" and "B" amounts, and because the current hold harmless provisions expire in FY 1973, limiting analysis in this manner seemed appropriate. Restricting analysis to changes in Tier 2 payments seems reasonable because it has been the intent of the Congress to fund at this level in FY 1976 through FY 1978. Given this policy of Tier 2 funding, comparisons based on Tier 3 amounts would result in overstatements of funding levels for some districts (e.g., those with public housing children).

the effects of each individual option presented. No attempt is made to combine reforms. Because of the often complex interrelationships among the various parts of the program, it would be very misleading merely to add up the effects of the options. Consequently, Section IV will combine selected options into reform packages designed to illustrate more comprehensive approaches for reforming the program.

Modifications Affecting the Types of Children for Whom Payments Are Made and the Way Payment Rates Are Calculated

As we have seen, the present program allocates funds using a formula which counts each district's Federally connected children (weighted to reflect the relative amount of burden each represents) and multiplies this count by a payment rate which is intended to approximate the portion of per pupil costs that would have been paid from local revenues had Federal impact never occurred. Although past investigators have examined other payment strategies (e.g., direct Federal tax payments, net burden compensation) and often have considered the present per pupil payment formula a less than ideal way to calculate entitlements, most have generally concluded that, all things considered, the present arrangement is the

most technically and politically feasible method available.[1/] It is for this reason that the reform options affecting the present program's compensation system focus on changing the kinds of children who are counted for entitlement purposes and the methods used to determine local contribution rates, rather than on the form of the compensation formula itself.

Reform Options Affecting Types of Federally Connected Children for Whom Payments Are Made

Under present law, entitlements are based on the number and type of Federally connected children who attend school in a recipient district. As has been noted, districts may now claim entitlements for over a dozen different categories of children, some of whom, it is argued, represent no burden on the district or only a small burden. Because of the somewhat ambiguous nature of the losses created by such children, many have

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1/ For example, Battelle's analysis of the program notes that "The ideal entitlement formula would calculate the total costs of education in the district, subtract the total costs that would have been incurred if there had never been a Federal impact on the district and pay the difference between those costs after subtracting the added revenues made available from Federal activity. These added revenues would be derived by taking the actual revenues of the district and subtracting what those revenues would have been had there never been a Federal impact on the district, but had the district continued to levy the same tax rate as it currently does." However, Battelle goes on to note that unfortunately this formula is unworkable because there is no correct way to estimate what either the costs or revenues would have been had there never been a Federal impact on the district. See Battelle Memorial Institute, School Assistance in Federally Affected Areas, 1969, pp. 84-85.

suggested reforms that would merely eliminate or reduce entitlements for all but the most burdensome categories.

Several of these entitlement reform options were investigated as part of this study. (See Figure 1 for an overview of these). The most far-reaching would eliminate entitlements for all "B" category children. This reform was proposed by the current Administration in FY 1978 and by several previous ones as well. It is generally justified on grounds that children whose parents live or work on Federal property, but not both, represent much less of a potential revenue loss for a district than children whose parents live and work on non-taxable Federal property.

Opponents of this measure argue that it is a severe one which eliminates entitlements for many justifiable "B" category children. Among these opponents, those sympathetic to reform argue for changes that are more selective and less extreme.

Several such reforms were investigated. The harshest of these examined the impact on payments of eliminating entitlements for all but the most unambiguously burdensome "B" category children -- those whose parents are in the uniformed services or who are civilians living on (non-public housing) Federal property.

Since it can be argued that there is at least a partial tax loss associated with children whose parents work but do not live on Federal property -- a loss that would go uncompensated

FIGURE 1: Overview of Reform Options Affecting Types of Federally-Connected Children for Whom Payments Are Made

Option	Description	Pro/Con
1	ELIMINATE PAYMENTS FOR ALL "B" CATEGORY CHILDREN.	Pro . Would retain payments for most burdensome "A" category children. Con . Harshest reform examined; eliminates over 4,100 districts and reduces payments by over 50 percent of current Tier 2 level. . Eliminates payments for lightly and heavily impacted districts alike. . Has been proposed and rejected in the past because it would eliminate payments for many justifiable children (e.g., military "B's")
2	ELIMINATE PAYMENTS FOR ALL "B" CATEGORY CHILDREN EXCEPT THOSE WITH PARENTS IN THE UNIFORMED SERVICES AND THOSE WITH PARENTS WHO LIVE BUT DO NOT WORK ON FEDERAL PROPERTY	Pro . Would retain payments for "A" children and most burdensome "B" children. Con . Although less harsh than Option 1, still eliminates payments for many "B" children who are a burden on the district. . Eliminates 441 districts and reduces Tier 2 payments by about 40 percent. . Eliminates payments for lightly and heavily impacted alike.
3	ELIMINATE PAYMENTS FOR "B" CATEGORY CHILDREN WHOSE PARENTS WORK ON FEDERAL PROPERTY IN A COUNTY OTHER THAN THE ONE IN WHICH THE DISTRICT IS LOCATED	Pro . Eliminates payments for least burdensome "B" children. Parents of these children work on Federal property in another district. The property would be untaxable to the district even if it were not Federally owned. . Option is logical extension of 1974 reform which eliminated payments for out-of-State"B" children Con . Without Federal presence, these children might live in another district. . Even though tax loss occurs for adjacent district, district of residence experiences a service burden because it must educate.
4	ELIMINATE PAYMENTS FOR PUBLIC HOUSING CHILDREN	Pro . Public housing is locally owned. Federal government does not require that communities construct these units. . Federal government already provides subsidies and in-lieu-of-tax payments for this property. . More efficient and appropriate means exist whereby the special educational needs of children in these units can be met. Con . By subsidizing public housing, Federal government may draw these high need children into a district. . Eliminating these payments would adversely affect center city districts which are already hard-pressed for resources. Payments to these districts would be reduced by over 30 percent.

under the preceding reforms -- more selective modifications which would only eliminate entitlements made on the basis of the most questionably burdensome types of children were also investigated. Specifically, two such reforms were examined: one which eliminated payments based on entitlements to public housing children (both "A" and "B" public housing students were eliminated), and a second which eliminated payments resulting from entitlements to children whose parents work on Federal property located outside the county in which the district is situated (i.e., entitlements for "B-out" children). It would have been desirable to test a reform which eliminated entitlements for all children whose parents work on Federal property in another district, not just those in another county; however, lack of data precluded such an assessment.

Reform Effects

The fiscal impacts associated with implementing these reform components are summarized in Table 14. The table shows FY 1976 Tier 2 "A" and "B" full reform payments for districts classified by degree of impact, metropolitan status, and property wealth, as well as the percentage reductions in these amounts that would result from each of the four entitlement reform options.

All of the reforms would result in some reduction in total costs. Reductions range from a low of about 5 percent ($25 million) when entitlements for "B-out" children are eliminated) to a high of over 50 percent ($273 million) when all "B"

TABLE 14: Percent Reductions in Full Reform "A" + "B" Payments Resulting From Reforms Affecting Children For Whom Payments Are Made

District Characteristics	Fully Reformed FY76 Through Tier 2		REDUCTIONS INCURRED AFTER IMPOSING REFORM							
			Eliminate All B's		Elim.All B's Except Mil. & Civ. Live-On Children		Eliminate Out-of-County Payments		Eliminate Public Housing	
	# of Districts (1)	A + B Payments (2)	# of Districts Eliminated a/ (3)	% Change in A+B Payments (4)	# of Districts Eliminated a/ (5)	% Change in A+B Payments (6)	# of Districts Eliminated a/ (7)	% Change in A+B Payments (8)	# of Districts Eliminated a/ (9)	% Change in A+B Payments (10)
ALL SAFA DISTRICTS.....	3,876	$512,336.62	2,125	-53.29	441	-39.50	64	- 4.96	43	-10.58
Percent SAFA Pupils										
75 - 100	99	$ 75,730.04	2	- 3.52	1	- 2.71	1	- 0.04		
50 - 74	108	51,476.38	9	-21.57	5	-14.20		- 0.16		- 0.21
25 - 49	406	132,952.73	79	-49.74	18	-31.55	1	- 2.93	1	- 2.17
15 - 24	480	95,268.97	190	-68.65	41	-46.83	7	- 6.43		-10.16
10 - 14	565	79,283.78	277	-79.85	70	-67.74	10	- 6.70	5	-35.16
5 - 9	1,245	49,267.90	833	-82.10	176	-66.85	24	-11.33	20	-16.98
Less Than 5	973	28,356.78	735	-84.62	130	-69.85	21	-15.48	17	-18.77
Metropolitan Status										
Central City	252	$141,130.16	111	-73.59	7	-59.62		- 3.25	3	-31.33
Suburban	1,045	167,996.89	700	-60.34	92	-39.88	5	- 7.86	13	- 3.09
Non-Metropolitan b/	1,938	183,235.95	1,047	-34.13	232	-25.76	46	- 3.82	26	- 2.56
Unclassified a/	641	19,973.60	267	-26.48	110	-20.17	13	- 3.12	1	- 0.61
Property Per Pupil c/										
Lowest Quartile	898	$163,926.24	505	-43.70	84	-30.27	12	- 3.28	6	- 3.70
2nd Quartile	799	106,568.39	470	-66.14	72	-45.07	9	- 6.20	13	- 9.28
3rd Quartile	696	73,749.29	404	-67.01	82	-45.50	13	- 9.50	14	- 8.29
Highest Quartile	673	83,902.25	385	-74.07	68	-65.06	11	- 6.01	9	-35.90

a/ Districts are considered to be eliminated when A+B payments equal zero. The eligibility criteria of 3 percent or 400 Federally connected children were not reapplied after the reforms.
b/ These districts could not be classified by metropolitan status. However, most are small and thus likely to be non-metropolitan in character.
c/ Districts are classified on the basis of within-State rankings.

SOURCE: 1976 SAFA Program Data Matched with 1970 Census (Metropolitan Status) and 1974-1975 Equalized Property Data (Property Per Pupil)

category entitlements are eliminated. As may be seen, eliminating entitlements for all but military and civilian (non-public housing) "B" children would result in the next highest reduction (about 40 percent of FY 1976 payments), while eliminating public housing entitlements would result in program savings of about 10.5 percent.

Table 14 also shows the estimated number of districts that would be eliminated from the program under each of the reforms.1/ Once more, eliminating all "B" category entitlements would have severe effects. Almost 55 percent (about 2,125 districts) of all recipient districts examined would be eliminated due to this option. Eliminating entitlements for all but the most burdensome "B" children would eliminate the next largest number of districts (about 441 in all), while the remaining reforms would have relatively negligible effects on this measure of reform impact.

1/ Districts were considered eliminated when "A" and "B" payments would be zero as a result of the reform. The current program's eligibility criteria were not reapplied. Reapplication of these criteria would result in substantially greater losses of districts and dollars:

Eliminate All B's		Elim. All B's Except Mil. & Civ. Live-on		Elim. Out-of-Co. Payments		Elim. Public Housing Payments	
#Dist. Elim. (1)	%Chg.in A+B Pay. (2)	#Dist. Elim. (3)	%Chg.in A+B Pay. (4)	#Dist. Elim. (5)	%Chg. in A+B Pay. (6)	#Dist. Elim. (7)	%Chg.in A+B Pay. (8)
3,041	-55.53	2,642	-42.19	649	-5.74	491	-11.39

Because aggregate figures hide important impact patterns, the distribution and magnitude of reductions across different types of districts are also of interest when evaluating these reform options.

For example, one of the severest criticisms that might be leveled against the reform which eliminates all "B" category entitlements is that it results in relatively large reductions for heavily and lightly impacted districts alike. Poor districts as well as wealthy ones experience large losses from this reform and, as may be seen, payments to central city districts are almost entirely eliminated. Similar observations might be made regarding the reform option which eliminates entitlements for all but the most burdensome "B" category children, although, as one would expect, losses to poor, heavily impacted, and city districts are somewhat lower than when all "B" payments are eliminated.

Reductions resulting from the public housing and "B-out" reform options seem much more equitably distributed in terms of degree of Federal impact and property wealth, with lightly impacted and wealthy districts bearing the brunt of the reductions. However, the public housing reform results in a disproportionately large reduction in central city district payments. Given the present fiscal difficulties of these districts, this may be a criticism of the reform; however, the results were not unexpected, since most public housing projects are located in these city districts.

Each of the four reforms which have been examined attempt to establish the principle that the Federal government's responsibility should extend only to students who represent a genuine Federal burden on their districts. Of these options, the first two are the harshest and, in our

opinion, the least justified since they indiscriminately eliminate payments for many children who do represent a genuine Federally imposed burden. The last two reforms are more selective and eliminate payments for children whose Federal burden on a district is more questionable. Making payments for children whose parents work on Federal property in another district is a practice that is difficult to justify and should be reconsidered. Eliminating payments for public housing children also makes sense, but will be more difficult to accomplish. Although these children do not represent a burden in the Impact Aid sense, they often are educationally disadvantaged and in need of special assistance. Moreover, eliminating public housing payments will have its most adverse effect on center city districts whose current fiscal difficulties are well known. Implementing this reform may thus well be impossible unless the legitimate claims of these children and their districts are addressed through increased efforts in programs like Title I, ESEA -- programs which are designed to deal more effectively with the real educational problems of these groups.

Reform Options Affecting the Way Local Contribution Rates Are Calculated

The preceding section dealt with reforms that would improve compensation by eliminating entitlements for children who are not a Federal burden or who are less of one than others. This discussion examines reforms that would alter the way local contribution rates are calculated. The changes we will examine are intended to improve

compensation for Federal burden by more accurately approximating a district's average per pupil costs of educating Federal students or by better approximating what per pupil educational expenditures (or revenues) would be if the district were not Federally impacted. As will become clear, none of the reforms presented here is optimal from all standpoints, but each responds to a specific set of criticisms of existing methods. Thus, any final selection among these options must depend on the balance that is struck between competing factors.

Figure 2 offers a schematic overview of the four reform options to be considered. Two points stand out: All options would restrict or eliminate the comparable district method, and three of the four would also dispense with the one-half U.S. average method. Perusal of the "Remarks" column of Figure 2 will also serve to illustrate our previous comment about competing factors. These include reasonableness of assumptions regarding Federal impact on district expenditures and/or revenues, distributional effects relative to district wealth and burden, evenhandedness with respect to different State school finance systems, and ease of program administration.

As may be seen from Figure 2, the first option examined represents perhaps the most modest reform that might be made to the present system. It would refine comparable district selection criteria and tighten up on Federal review and approval procedures while restricting the use of the method to heavily impacted districts (i.e., districts where "A" category children and/or "B" category children whose parents reside, but do not

FIGURE 2: OVERVIEW OF OPTIONAL LOCAL CONTRIBUTION RATE REFORMS

Option	EFFECTS OF OPTIONS ON METHODS OF CALCULATING LCR's:			REMARKS			
	Comparable District	1/2 State	1/2 U.S.	Reasonableness	Distributional Effects	Evenhandedness	Administrative Ease
1	Restrict use to districts where "A" and live-on "B's" are at least 50% of total ADA	(Retain both minimums for moderately and lightly impacted districts)		Imperfect approximation, but option does reduce likelihood of excessive compensation for districts that are well-to-do in spite or because of Federal activity.	Modest overall reductions. Progressive on wealth. Partially progressive on percent Federal children.	Not evenhanded--favors districts in high State aid/low expenditure States more than others.	Involves stricter monitoring of comparable district method, but for fewer districts.
2	Restrict as above.	Automatic for all but high impact districts as defined under Option 1.	Eliminate	Preferred to Option 1. Nationally about 1/2 all State education expenditures are derived locally. Assumes 1/2 State average is a reasonable estimate of what average district costs would be without Federal impact. Imperfect because does not adjust for expenditure differences between or within States. Otherwise, Option 1 comments pertain.	Largest across-the-board reductions. Reductions are nevertheless progressive on wealth and partially so on percent of Federal children.	From one perspective, more evenhanded than Option 1, but still favors districts in high State aid/low expenditure States. Although these districts lose, they lose less than if they were being compensated on basis of State avg. expenditures. Conversely, districts in low State aid States are under-compensated.	Same remarks apply as for Option 1.
3	Eliminate and replace with rate based on State's avg. local expenditures.	Retain as basic minimum for districts not using State avg. local expenditure method.	Eliminate	Makes reasonable assumption that without Federal impact district costs would be about equal to their State's avg. local expenditures. Imperfect because does not adjust for cost differences between districts in same State. Option 1 comments also apply.	Results in relatively large overall payment reductions. Reductions are highly progressive on wealth & partially progressive on burden if one disregards option's effect on payments to one unique, heavily impacted district in Alaska.	Option is evenhanded. State avg. local expenditure method is a reasonable substitute for comparable district method in low State aid States. 1/2 State avg. minimum is a generous de minimus for high State aid State districts.	Administratively the most simple option to implement.
4	Eliminate and replace with rate determined by multiplying each district's revenue effort times its State's avg. local property wealth per pup pupil.	Modify to guarantee 1/2 average revenues in the State and retain as a basic minimum for districts not using "tax effort" calculation method.	Eliminate	Makes reasonable assumption that without Federal impact district wealth would be about equal to State's avg. Imperfect because it does not account for effect of other service demands on wealth of certain districts (e.g. cities). Option 1 comments also apply.	Smallest overall reductions of all options examined. Although poor quality data preclude definitive assessment, appears to be most highly progressive of all options on wealth and relatively progressive on burden.	Option is generally evenhanded and equalizing.	Most difficult of all options to implement. Would require collection of accurate up-to-date property wealth and revenue effort data for all participating districts.

work, on non-public housing Federal property comprise at least 50 percent of total enrollment). All other districts would be required to calculate their LCR's using the higher of the two current minimum methods.1/

The principal justification for this option is that forcing lightly and moderately impacted districts to use one of the two minimum calculation methods reduces the likelihood that districts which are relatively well-to-do despite Federal impact or whose financial characteristics have been improved by Federal activity will use these as a means of increasing their Federal grants. Because heavily impacted districts are generally unambiguously burdened by Federal activity, the possibility that they will be able to take similar advantage of the comparable district method is less likely (or at least the thought that they might do so is somehow less distasteful). For this reason these

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1/ Many contend that the most straightforward modification that could be made to improve the present compensation system would be to leave it more or less intact while refining comparable district selection criteria and tightening up on Federal review and approval procedures. This was essentially the approach recommended by GAO after it found that current selection instructions and review procedures provide no assurances that districts selected are, in fact, comparable or that the rates calculated are reasonable. While the proposal to "clean up" the program has merit and, in fact, would be adopted for heavily impacted districts using the method under Options 1 and 2, we do not believe the strategy is sufficient by itself. In effect, we feel that the comparable district method is inherently defective because it requires the selection of districts comparable to the type of community the district became as a result of Federal impact, rather than to what the community would have been had the impact not occurred. Moreover, merely "cleaning up" the comparable district method will do nothing to correct compensation errors which presently result from minimum calculations which are equally imprecise.

districts are permitted to continue their use of the comparable district method. Essentially, Option 1 makes a judgment that, to the extent that they occur, comparable district compensation errors which favor high impact districts are more acceptable than those that benefit districts which are less clearly burdened and, in fact, may have been helped once already.

Although this first reform option moves away from the practice of compensating districts on the basis of characteristics acquired as a result of Federal activities, the fact that it permits some lightly and moderately impacted districts to continue calculating their rates by selecting the current national minimum method may irritate those who believe that the program is intended primarily to offset the added local costs of educating Federally connected children. Although one could maintain that considerations of inter-State equity argue for retention of the national minimum calculation method, critics will correctly note that the Impact Aid program is concerned primarily with compensating for reduced district expenditures or revenues, and that its scope and coverage are too narrow to deal effectively with equalizing expenditures or revenues across States. These critics will justifiably argue that by offering a minimum calculation method based on the national average, Option 1 merely perpetuates an inequity of the current program: that districts in low expenditure States are compensated directly for low overall spending levels, while districts in high expenditure States, where costs are generally above average, are not extended a similar courtesy.

In effect, one could contend that if the national minimum method is appropriate, then so too is a cost of education formula adjustment.

The second option addresses these criticisms. Basically, this reform is the same as Option 1, except that rather than permitting lightly and moderately impacted districts to select from between the two current minimum calculation methods, it requires these districts to use the current State average method. Because, on average, about one-half of all State education expenditures are derived from local revenue sources, this option moves a step closer toward the goal of compensating districts for increased local costs. By eliminating the national average calculation and restricting use of the comparable district method, the option also moves away from several practices which result in inflated approximations of what district costs would have been in the absence of Federal impact.

Critics of this option will note that while it does eliminate practices which result in the most significant overcompensation for districts, it creates new problems of its own. In particular, while it is true that nationally about one-half of all State education expenditures are locally derived, in fact, like most averages, this one overestimates the percentage in some States and underestimates it in others. Put another way, basing district LCR's in all States on a national average fails to adjust for expenditure differences between and within the States. Thus, while districts in high State aid/low expenditure States will generally find their rates somewhat reduced by this option, they will also

continue to receive higher amounts than if they were being compensated exclusively on the basis of average local expenditures in their States. Conversely, districts in States where at least one-half of all education expenditures are derived from local sources will be compensated at lower than State average rates. In effect, although Option 2 is more evenhanded than Option 1 because it eliminates the national average floor for districts in low expenditure (generally low local aid) States, critics will note that it too results in an imperfect set of approximations for what district expenditures would have been in the absence of Federal impact.

The last two LCR reform options to be examined eliminate the comparable district method entirely and move toward compensation schemes which utilize the local expenditure and revenue patterns in each State to more perfectly approximate what district costs would have been had Federal impact not occurred. The first of these, Option 3, would set a district's local contribution rate at either its State's average local expenditures per pupil or at one-half its State's average non-Federal expenditures per pupil, whichever is higher.[1/] This option was chosen because of its

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1/ "State average local expenditures" were calculated by multiplying local elementary and secondary school current operating expenditures by the percentage which local revenues were of total revenues in the State. This product was divided by State ADA to obtain a per pupil amount. Since FY 1976 SAFA payment rates are based on FY 1974 data, revenues, expenditures and ADA are also for FY 1974.

administrative simplicity and because, not unreasonably, it assumes that had Federal impact not occurred, district per pupil expenditures would be about the same as the current average for the State. The one-half State average calculation method was included to provide districts in high State aid/low expenditure States with more compensation than they would receive were average local expenditures used exclusively. In effect, it was judged that as a deminimus payment mechanism, the State average method yields more reasonable approximations of what these districts' costs would have been without Federal impact than does the U.S. average method.

For many, the major problem associated with this option will be that what it gains in simplicity comes at the expense of failing to reflect differing situations throughout the State. In effect, many will prefer an option that allows payments to vary with each district's expenditure or revenue effort for education.

The final LCR reform examined in this section would partially address these criticisms. Originally proposed in the Battelle Study, Option 4 would guarantee each district its State's average per pupil property base. Local contribution rates would then be determined by multiplying this State average property base by the district's own revenue effort rate. According to Battelle, this option has several benefits:

> "...it makes a very reasonable assumption about the likely situation in the district assuming the Federal government has never had an impact on it. In effect, it presumes that in the absence of Federal impact the district would tend to have had a tax base per pupil about like the current average in the State. This approach is preferable to giving the district credit or blame for Federal impacts that tend to reduce or increase tax base per pupil. This assumption is more likely to be true than the one inherent in comparable districts...(which requires)...the selection of districts comparable to the type of community the district became..., not districts comparable to what the community would have been had the Federal impact not occurred."1/

A second advantage is that this option guarantees that no district can increase its LCR merely by manipulating the method of calculation. As Battelle notes, "The only way that a district could raise its Federal payments is to convince the local voters or political decisionmakers that additional expenditures are necessary."2/

Critics of this option will note that it has several major drawbacks. First, it fails to adjust for the effects of other service demands and higher costs on the wealth and fiscal capacity of certain districts. That is, while many may prefer this option over the others, they will also note that it still only imperfectly adjusts for different local circumstances, particularly the higher

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1/ Battelle Memorial Institute, School Assistance in Federally Affected Areas, 1969, pp. 94-196.

2/ This may be a disadvantage as well. A predominantly Federal district, (for example, one with a 90 percent "A" category enrollment) might find it advantageous to raise tax rates in order to increase Impact Aid payments. Assuming that such an action was not prohibited by State or local laws, doing so would cost the Federal majority very little. It could, however, result in disproportionate cost increases for the civilian minority. Many will consider this inequitable.

costs and non-educational service burdens that affect revenue efforts and fiscal resources in center city districts. While our analysis has not dealt directly with this criticism, we agree that it is a legitimate issue and an appropriate topic for future study -- one that needs to be addressed for this and all other options which rely on average values to calculate compensation rates.

This option has at least one other major drawback which we have addressed. Specifically, it is not neutral in the way it treats different, but equally valid, State school finance arrangements. Thus, although districts in States which finance a large portion of their education costs from local sources are likely to do fairly well under this option, those that are in States which defray a large portion of education costs by tapping State resources are likely to receive smaller compensation rates than under the present system. One could argue that this is entirely appropriate, since the Impact Aid program is intended only to compensate for losses in local capacity. On the other hand, some minimum for these districts is a political necessity. Hence, we have retained a revenue based version of the State average minimum calculation method (i.e., we guarantee at least one-half State average non-Federal revenues) as an alternative that will provide relief for districts in high State aid States. We have done this realizing

that some will justifiably complain that by doing so we may be overcompensating some of these districts in the bargain.1/

LCR Reform Effects

Table 15 shows how each of the various reforms which restrict or eliminate the current calculation methods would affect each State's SAFA payments. The table indicates that all of the reforms result in overall funding reductions. As may be seen, Option 1, which restricts use of the comparable district method to high impact districts but retains both current minimum calculation methods, reduces "full reform" SAFA payments from $512.3 million to $478.7 million (i.e., about 6.5 percent). Lightly to moderately impacted districts in States which are high spenders and/or rely largely on locally raised revenues to support education appear to be the most adversely affected by this reform. For example, Massachusetts, New Jersey, New Hampshire, and Oregon (States where districts depend heavily on the comparable district method) all experience payment reductions of between 15 and 44 percent. In some other States (e.g., Illinois and New York), losses appear to have resulted because a few major center city districts which account for large proportions of their States' Impact Aid grants are prohibited from

1/ For this option, district and State revenues have been adjusted to reflect only that portion of total non-Federal revenues raised for current operating purposes. That is, both district and State non-Federal revenues have been multiplied by the proportion of current operating expenditures to total State expenditures.

TABLE 15: Percentage Changes in Fully Reformed FY 1976 Tier 2 Level SAFA "A" and "B" Payments Resulting From Alternative LCR Reform Options -- States (see text for detailed explanation of reform options)

District Characteristics	Districts in Sample (1)	'76 Tier 2 A+B Full Reform Payments (Thousands) (2)	Percent Change From: LCR Reform Option 1 (3)	LCR a/ Reform Option 2 (4)	LCR Reform Option 3 (5)	LCR Reform Option 4: Districts in Sample (6)	'76 Tier 2 A+B Full Reform Payments (Thousands) (7)	Percent Change From Option 4 (8)
Grand Totals.....	3,876	$ 512,334	- 6.57	- 15.28	- 12.87	1,885	$ 371,158	- 0.47
*Alabama	81	$ 8,092	0.00	- 31.75	- 31.75	50	$ 7,217	- 38.75
*Alaska	29	39,302	0.00	0.00	- 48.10	0	NA	NA
Arizona	105	19,240	- 0.97	- 7.69	- 8.29	21	4,104	85.79
*Arkansas	93	3,002	0.17	- 30.13	- 37.70	41	2,792	- 36.80
California	447	60,528	- 2.77	- 5.07	5.24	191	45,557	30.73
Colorado	84	10,958	- 8.79	- 13.33	- 8.91	49	10,266	- 0.62
Connecticut	30	3,819	- 20.20	- 20.20	- 6.90	23	3,749	5.91
*Delaware	4	375	0.00	0.00	0	4	375	27.15
District of Columbia	1	3,727	0.00	0.00	33.15	0	NA	NA
*Florida	25	18,175	0.00	- 12.80	- 12.80	22	18,054	4.38
*Georgia	76	10,050	0.00	- 28.53	- 28.53	33	9,100	- 21.40
*Hawaii	1	12,592	0.00	0.00	0	0	NA	NA
Idaho	64	3,522	- 0.33	- 28.64	- 28.64	34	3,136	- 26.92
Illinois	149	13,457	- 19.38	- 19.38	- 9.13	66	10,802	5.25
Indiana	35	1,938	- 0.57	- 15.09	- 14.38	26	1,841	23.09
Iowa	28	509	- 0.90	- 6.39	- 0.45	10	196	50.63
Kansas	68	6,656	- 3.77	- 8.99	- 9.95	38	5,023	13.81
*Kentucky	61	2,512	0.00	- 37.25	- 37.25	32	2,155	- 23.65
*Louisiana	21	3,833	0.00	- 19.65	- 19.65	21	3,833	- 12.39
Maine	65	2,340	0.00	- 15.51	- 15.64	33	2,016	22.06
Maryland	14	20,191	- 15.87	- 15.87	- 15.87	14	20,191	- 3.19
Massachusetts	94	5,267	- 15.96	- 15.96	10.48	63	3,303	60.08
Michigan	63	6,213	- 2.38	- 2.38	- 2.38	25	2,443	9.10
*Minnesota	39	2,881	0.00	0.00	0	20	1,553	6.02
*Mississippi	36	3,460	0.00	- 41.36	- 41.36	21	3,302	- 37.17
Missouri	129	6,519	- 2.70	- 11.33	- 0.95	53	3,738	15.91
Montana	126	6,475	- 4.27	- 5.60	8.12	27	1,762	- 0.80
Nebraska	25	5,617	- 23.19	- 28.47	0.40	15	4,945	69.28
Nevada	14	4,002	0.00	- 8.48	5.85	12	3,969	- 9.47
New Hampshire	28	1,673	- 44.35	- 51.84	- 14.86	14	1,598	3.36
New Jersey	131	12,976	- 25.20	- 25.20	8.13	81	12,203	- 29.15
*New Mexico	61	17,648	0.00	- 10.91	- 19.75	29	15,769	- 21.21
New York	146	31,678	- 21.88	- 21.88	- 8.53	91	28,839	- 17.44
*North Carolina	62	3,667	0.00	- 23.24	- 23.24	53	8,373	- 11.47
North Dakota	67	4,957	0.00	- 13.50	- 14.18	20	3,203	12.90
Ohio	108	8,974	- 11.97	- 21.93	0.79	64	7,525	- 5.03
*Oklahoma	328	12.726	- 0.10	- 25.88	- 26.67	71	7,310	- 22.35
Oregon	86	3,036	- 26.91	- 26.91	5.53	33	2,100	2.14
*Pennsylvania	100	8,680	- 8.37	- 8.37	- 8.37	78	8,323	- 0.27
Rhode Island	12	1,658	- 12.58	- 12.58	- 1.18	12	1,658	5.00
*South Carolina	22	7,784	0.00	- 29.15	- 29.15	13	7,682	- 32.13
South Dakota	50	6,005	- 4.88	- 11.35	- 0.36	44	5,828	11.95
*Tennessee	89	6,945	0.00	- 32.14	- 30.14	64	5,769	- 21.56
*Texas	232	30,836	0.00	- 23.11	- 27.56	88	22,817	- 10.04
*Utah	34	7,372	0.00	- 25.36	- 25.36	25	7,161	- 14.36
Vermont	15	88	- 10.07	- 12.31	14.13	13	81	99.22
Virginia	64	34,131	- 19.6%	- 29.60	- 20.07	42	33,433	- 1.12
*Washington	158	15,734	- 0.46	- 0.46	- 0.82	53	11,566	13.13
*West Virginia	12	438	0.00	- 27.36	- 27.36	12	438	- 25.70
Wisconsin	39	1,995	- 7.11	- 7.11	9.06	18	1,008	12.29
Wyoming	25	3,088	- 8.51	- 8.51	- 12.57	23	3,058	13.48

a/ To simulate this option, LCR's for heavily impacted districts were retained. Even though some of these districts are not now using the comparable district method, the option gives these districts latitude to use it and thus retain or raise their current compensation levels. A more conservative methodology, which was rejected, would have assigned high impact districts not now using the comparable district method a rate equal to one-half their State's average non-Federal expenditures per pupil.

NA -- Not Applicable

* -- State finances at least half of all education costs.

SOURCES: Reform Options 1-3, 1976 SAFA Program Data Files (Average Local Revenues Used for Option 3 Derived from 1974-1975 ELSEGIS Data File).

Reform Option 4, 1974-1975 ELSEGIS -- 1976 SAFA Program Data Matched File.

using the comparable district method to calculate payment rates. In general, this reform option seems to have its greatest impact on districts in large high spending (high cost) urban States, especially those in the Northeast.

Although Option 2 differs from Option 1 only by eliminating the U.S. average minimum calculation method, its impact is much greater, resulting in a funding reduction of over 15 percent (i.e., SAFA "full reform" monies drop from $512.3 to about $434 million). This result was predictable; over half of all SAFA districts rely on the U.S. minimum calculation method eliminated by this reform, and about 49 percent of all SAFA monies are distributed on this basis.

The effects of moving from Option 1 to Option 2 are additive. That is, districts which lose under Option 1, lose as much or more under Option 2. The geographic distribution of these losses changes greatly, however. Specifically, districts in most Southern and border States -- those which were generally unaffected by the first reform option -- are among the most adversely affected by the second. As we have noted previously, these States have had historically low levels of non-Federal spending for education and are traditionally high State aid States which rely on the U.S. minimum method that is eliminated by this option.

In general, this reform works to the disadvantage of districts in all but a few States like Delaware, Minnesota, and Hawaii -- States which already rely exclusively on the State average minimum.

Table 15 shows that implementing Option 3 would reduce overall funding by about 13 percent (i.e., "full reform" payments would decline from $512.3 to $446.4 million). The principal beneficiaries of this option would be many of the heavy losers under Option 1 -- i.e., districts in high local aid and/or high expenditure (or high cost) States like Massachusetts, New Jersey, and Vermont. For the most part, these districts would be able to take greater advantage of their relatively high local contributions for education than they are now permitted using present calculation methods.

The major losers under this reform are districts in Alaska and most Southern and border States. Alaska's 48 percent loss is somewhat misleading, however, since it is due entirely to reduced payments in one heavily impacted district. Without reform this district would receive over $2,200 for each of its 14,000 "A" category children; with reform the district receives only about $968 for these same students. Other Alaskan districts would neither gain nor lose under reform, because they would be permitted to retain their current payment rate, which is based on the program's State average minimum.

Southern and border State districts lose under this option because of their overall low expenditure levels and because of their heavy reliance on State education aid. That is, average locally financed expenditures in these States are so low that most districts would have to calculate their rates on the basis

of the current State average minimum method. Because this method yields LCR's which are generally lower than those resulting from the national average minimum method (which districts in these States currently use), payments decline dramatically.

Although the major gainers under Option 3 tend to be districts in States where local aid is high relative to State aid, some of these districts also experience losses from the reform. Again, most of these losses accrue to districts in States with low overall levels of expenditure for education -- States like Idaho and Maine where districts currently rely exclusively on the program's national average minimum to boost their rates well above State average local expenditures.

If one agrees that State average local expenditures are a reasonable estimate of what districts would have been spending had Federal impact never occurred, the results shown in Table 15 for Option 3 also provide some suggestions regarding the extent to which the comparable district method accurately compensates for Federal burden. That is, if the comparable district method were providing a reasonable approximation of local education costs, then one would expect that payments to districts in States which rely heavily on this method would not be adversely affected by Option 3. In fact, our data show that when 10 States which use this method exclusively or disproportionately are examined, six lose as a result of reform (Iowa, Kansas, New Hampshire, Rhode Island, Wyoming, and South Dakota), but only three (Kansas, New Hampshire and Wyoming) lose by any

significant amount. Four of the 10 States gain from reform (Nebraska, New Jersey, Oregon, and Wisconsin), with two (Wisconsin and New Jersey) gaining significantly. In effect, given these results, the comparable district method seems to be compensating accurately in only about half the States. In the others it either overcompensates or undercompensates for Federal burden.

Table 15 also shows the geographic distribution of gains and losses resulting from Option 4. As may be seen, this option results in the most modest payment reductions of all LCR reforms. Total program dollars decline by less than one-half of 1 percent -- from $512.3 to $509.9 million.

The major gainers under this option are districts in low State aid States like Arizona, Massachusetts, and Vermont. Districts in these States apparently gain because of their relatively high local revenue efforts for education.

Not surprisingly, districts in Southern States like Alabama, Arkansas, Mississippi, and South Carolina are the principal losers under this option. These are high State aid/low wealth States, and districts located in them lose because these two factors combine to yield lower compensation rates than those obtained currently using the program's national average minimum method. Districts in some high wealth/high local effort States also lose, apparently because rates calculated using Option 4 are lower than those obtained using the program's comparable

district method. Districts in New York and New Jersey are the most striking examples of this phenomenon. Their losses probably occur because this option reduces payments to the several large center city districts which dominate these States.

A somewhat different perspective on the effects of these reforms is provided in Table 16. It shows the percentage change in SAFA dollars resulting from each option for districts classified by degree of Federal impact, metropolitan status, and property wealth.

As may be seen, Options 1 and 2 result in across-the-board reductions for all types of districts, but affect some more drastically than others. Heavily impacted, non-metropolitan and low wealth districts lose least under both reforms, while moderately impacted, suburban, center city, and high wealth districts are the most adversely affected. In general, the pattern of losses is progressive in property wealth terms under both options, with districts experiencing larger losses as their wealth increases. This pattern is only partially repeated for districts classified by degree of Federal impact. That is, losses under both options tend to be progressive until they reach the 10-14 percent impact grouping. At this point the pattern deteriorates with losses declining for the two least heavily impacted categories.

Data showing the percentage of 1976 Tier 2 SAFA payments received by different types of districts from using the comparable district calculation method suggest why these losses occur

as they do (see Table 5). The data indicate that those districts which currently rely most heavily on the comparable district method are, as one might expect, the same LEA's which lose the most when the use of the method is restricted to heavily impacted districts. For example, given that districts in the 10-14 percent impact grouping derived over 62 percent of their 1976 Tier 2 Impact Aid money by using the comparable district method, it is not surprising that they should lose large amounts when prohibited from using it. Similarly, suburban, center city, and high wealth districts lose more than others because they tend to rely heavily on the comparable district method and are also more likely than other LEA's to be lightly or moderately impacted.

The combined effect of eliminating the comparable district and national average calculation methods from the program and substituting Option 3 in their place is shown in Column 5 of Table 16. As may be seen, the most striking difference between the first two options and the third relates to the latter's effect on payments to districts in the most heavily impacted category. In particular, whereas losses to these districts are relatively modest under the first two options (and primarily attributable to the net effect of eliminating the national average minimum calculation method), they are quite large under Option 3.

These losses may be attributed to two factors. First, Option 3 eliminates the comparable district method -- a method which generated over 60 percent of these districts' FY 1976 Tier 2 SAFA payments. Second, a large portion of the loss results from

payment reductions experienced by the one large heavily impacted Alaskan district discussed in previous sections. That this one district tends to dominate the high impact category is evidenced by what happens when it is omitted from the analysis. When this is done, the loss to heavily impacted districts declines from over 26 percent to only 2.6 percent. Similarly, when this district is omitted, the loss to non-metropolitan districts is cut in half (i.e., it declines from -18.2 to -9.6 percent).

Disregarding this one district, the patterns of funding change under Option 3 are not much different from those observed for Options 1 and 2. High wealth, center city, and moderately impacted districts continue to be the most adversely affected by reforms which use State averages to approximate what district expenditures would be without Federal impact; while low wealth, suburban, low impact and, for the most part, high impact districts are the least affected.

Table 16 also presents information about how Option 4 would affect funding for different types of districts. Unfortunately, due to technical difficulties associated with matching data from two different sources, we were able to simulate this option for only 1,885 districts (49 percent). While this sample accounts for a substantial 72 percent of all "full reform" SAFA dollars, it omits, among others, the large heavily impacted Alaskan district. Thus, even though our data are likely to be relatively reliable for most of the district categories we are examining, they are probably not very good for some. In particular, our

TABLE 16: Percentage Changes in Fully Reformed FY 1976 Tier 2 Level SAFA "A" and "B" Payments Resulting from Alternative LCR Reform Options: Selected District Characteristics (see text for detailed explanation of reform options).

District Characteristics	Districts in Sample (1)	'76 Tier 2 A+B Full Reform Payments (Thousands) (2)	Percent Change From: LCR Reform Option 1 (3)	LCR Reform Option 2 c/ (4)	LCR Reform Option 3 (5)	LCR Reform Option 4: Districts in Sample (6)	LCR Reform Option 4: '76 Tier 2 A+B Full Reform Payments (Thousands) (7)	LCR Reform Option 4: Percent Change From Option 4 (8)
Grand Totals.....	3,876	$ 512,334	- 6.57	- 15.28	- 12.87	1,885	$ 371,158	- 0.47
Percent SAFA Children								
75 - 100.....	99	$ 75,740	- 0.01	- 0.35	- 26.43	16	$ 12,594	+ 11.34
50 - 75.....	108	51,476	- 3.06	- 9.40	- 5.18	35	36,742	+ 7.16
25 - 50.....	406	132,952	- 4.16	- 16.50	- 9.14	174	104,138	- 0.85
15 - 25.....	480	95,269	- 8.86	- 20.62	- 13.46	198	80,269	- 7.04
10 - 15.....	565	79,282	- 16.65	- 23.63	- 16.10	254	71,205	- 12.16
5 - 10.....	1,245	49,267	- 5.68	- 16.97	- 7.40	621	40,753	+ 5.90
Less than 5.....	973	28,356	- 7.52	- 15.86	- 6.64	587	25,458	+ 11.68
Metropolitan Classification								
Center City	252	$ 141,130	- 9.33	- 18.61	- 10.51	227	$ 121,865	- 2.82
Suburban	1,045	167,996	- 9.37	- 17.78	- 9.72	751	151,014	+ 3.53
Non-Metropolitan	1,938	183,235	- 2.17	- 11.04	- 18.16	853	96,746	- 3.91
Unclassified a/	641	19,973	- 4.00	- 9.59	- 7.55	54	1,533	+ 9.80
Property Per Pupil b/								
Lowest Quartile	898	$ 163,926	- 3.06	- 12.06	- 4.66	519	$ 130,068	+ 9.50
2nd Quartile	799	106,568	- 4.18	- 16.16	- 8.15	475	96,722	+ 6.34
3rd Quartile	696	73,749	- 13.15	- 22.81	- 16.34	425	65,389	- 7.45
Highest 25%	673	83,902	- 15.72	- 25.43	- 19.80	403	76,956	- 19.90

a/ These districts could not be classified by metropolitan status. However, most are small and thus likely to be non-metropolitan in character.

b/ Districts classified based on within-State rankings.

c/ To simulate this option, LCR's for heavily impacted districts were retained. Even though some of these districts are not now using the comparable district method, the option gives these districts the latitude to use it and thus retain or raise their current compensation levels. A more conservative methodology, which was rejected, would have assigned high impact districts not now using the comparable district method a rate equal to one-half their State's average non-Federal expenditures per pupil.

SOURCE: Options 1-3: Percent SAFA Data derived from 1976 SAFA Program Data Files; Metro Class derived from 1970 Census -- 1976 SAFA Program Data File match; Property derived from 1976 SAFA Program Data File matched with 1974-1975 Equalized Property Data (Average Local State Average Expenditures for Option 3 derived from 1974-1975 ELSEGIS Data File).

Option 4: Same as above matched with 1974-1975 ELSEGIS data on district revenues.

confidence in the data shown for districts with between 50 and 100 percent Federal enrollment and for rural and unclassified categories is not very high. As a result, the following analysis of Option 4 is brief and very tentative.

Based on the limited data at hand, it would appear that an LCR reform which guarantees all districts their State's average property base but allows payment rates to vary in relation to district revenue effort results in a progressive pattern of gains and losses for districts classified by property wealth. In effect, our results make it apparent that if all districts had equivalent property wealth but were permitted to calculate their compensation rates on the basis of individual revenue effort, then current payments to wealthy districts would decline, while those to less wealthy districts would increase. These findings tend to substantiate the claims of many Impact Aid critics who argue that the present program is too generous to wealthy districts whose revenues (and compensation rates) are high even though their revenue efforts are low.

Technical problems make it difficult to interpret results for districts classified by degree of Federal burden, especially as these pertain to districts in the two highest categories. This is particularly the case for the highest impact category, since our sample does not contain the one Alaskan district that we know dominates this grouping. One surmises that had our sample been more complete, gains to this category would have

been somewhat lower than shown -- primarily because of the effect the option would have on this one district's funding.

Disregarding for the moment these technical problems, it would appear that the fiscal impacts on districts classified by degree of Federal burden only partially conform to what one might expect if it were true that property wealth increases and tax effort decreases as the degree of Federal impact declines. That is, if these variables were highly interrelated, one might reasonably expect Option 4 to result in increased payments for heavily impacted districts and in progressively and substantially reduced payments for moderately and lightly impacted districts.

In fact, although the patterns of change are exactly what one might expect for districts in heavily and moderately impacted categories, payments actually increase for districts in the two most lightly impacted groupings. Since earlier we noted that these districts have about average property wealth per pupil, one can only conclude that tax efforts in these districts are higher than expected -- high enough to raise their payments above the amounts they receive using current calculation methods.

Insofar as this option can be considered an improvement over present calculation methods, it once more appears that major overpayments are currently being made to high wealth and moderately impacted districts, especially those with Federal enrollments of between 10 and 15 percent. Center city districts are also receiving higher levels of compensation under the present program

than they would under Option 4, although these payments do not appear to be excessively large. Given the poor quality of data that is available, it is impossible to draw any strong conclusions regarding heavily impacted and non-metropolitan district payments.

Perhaps the most meaningful conclusion that can be drawn from the preceding results is that although Option 4 has a relatively modest impact on the overall level of SAFA funding, it does seem to result in significant shifts in funding among different types of districts. In particular, poor districts, whether heavily or lightly impacted, seem to benefit, while wealthy ones that are moderately impacted lose.

As stated earlier, reforms examined in this section move away from the present practice of relying on biased or excessively inflated estimates of what district costs would be without Federal impact. They do this by restricting or eliminating use of comparable district and/or national average calculations and substituting in their place other methods based on the average revenue or expenditure patterns of individual States. Though none of these reforms is perfect, all achieve some measure of reform. Options 3 and 4 probably come closest of all reforms to achieving a balance between the competing factors described earlier. Both make reasonable assumptions about Federal impact, and both are relatively evenhanded with respect to

different State finance systems. Option 3 has the added advantage of being the easiest reform to implement -- a feature that recommends it over Option 4, which is by far the most administratively difficult of all reforms examined. On the other hand, disregarding for the moment that our data are incomplete, it would appear that if distributional effect is a major selection criterion, then for the most part Option 4 is the more appealing of the two.

Options 1 and 2 do not measure up nearly so well on the basis of these criteria as Options 3 and 4. One suspects that this is primarily because both try to work with the current program's compensation mechanisms. Of the two, however, the second option makes the most reasonable assumptions regarding Federal impact and is also more evenhanded. Unfortunately, Option 2 is also the harshest of all reforms, a fact that will lead many to ignore it completely.

From our results one thing seems clear: Certain districts generally have more to fear than others from reforms that move toward improved estimates of Federal impact. By far, those with the most to lose are high wealth districts and districts which are moderately impacted. Districts located in low expenditure/high State aid States (especially those in the South), also have much to lose from reform.

Those which lose least from reform (or gain) are poor districts. Indeed, the one constant in all of these reforms is that they tend to be progressive on wealth. Heavily impacted

districts are also relative "gainers" from reform if one disregards reductions to the one unique Alaskan district which result from Option 3 (and probably Option 4). Surprisingly, districts in the two lowest categories of impact do better than expected under most reforms and even gain under Option 4. Finally, districts in high expenditure/low State aid States also do relatively well under most of the reforms examined, especially under Options 3 and 4, the reforms which most improve current arrangements.

Modifications to Achieve More Equitable Impact Aid Distributions to Districts

As has been demonstrated, the current program makes payments to lightly impacted districts that do not seem to be burdened by Federal activities and which may even benefit from their Federal connection. In 1976, such districts constituted over one-half of all eligible program recipients and received about 20 percent of all Impact Aid dollars. As we have noted, critics of the program argue that these payments overcompensate lightly impacted districts and represent a low priority use for scarce Federal resources. This section examines the present program's provisions for dealing with these problems and investigates how eligibility mechanisms might be strengthened to achieve a more equitable and efficient distribution of Impact Aid funds.

Although many have argued that Impact Aid compensation ought to extend to all Federally connected children in every affected school district, such claims have always been rejected. From the Federal perspective, universal eligibility conflicts with national education priorities and basic program goals. It is also administratively impractical. For example, many districts contain only three or four Federal students. Such districts have only a minor claim on Federal funds because in relative terms their burdens are small and can be easily absorbed from local resources. Making payments to these districts would be wasteful and impractical because the money could be better spent on those who really need support, and because the administrative costs involved in making these awards would likely be greater than the resulting payments.

The present program's eligibility requirements were enacted to prevent such payments. Specifically, the current program restricts participation to districts that have a Federal enrollment equal to at least 3 percent or 400 total children, whichever is less. If the 3 percent threshold is used, a district must have at least 10 Federal children to qualify. The 400 child threshold is essentially a concession to large city districts which would not qualify under the 3 percent minimum, while the conditional 10-child restriction limits participation by very small rural districts which would otherwise qualify under the 3 percent rule, even though they might have only one or two Federal children.

Although the present program's eligibility provisions solve the problem of making some deminimus payments, they may be criticized on several grounds. For example, they clearly do not prevent payments to "borderline" districts -- i.e., districts which are lightly impacted but just barely manage to meet the eligibility threshold requirements. That these districts receive as much Impact Aid money as they do stems largely from the current practice of paying qualifying districts for all Federal children. That is, once a district meets or exceeds one of the minimum thresholds, the program pays the districts for every Federal child, even those who are below the program's eligibility minimums.

Critics of the present program have correctly observed that because of these practices, Impact Aid eligible districts are treated very differently from ineligible districts even though the latter may have about the same number of children who are Federally connected. Thus, a district that barely meets the eligibility requirements of 3 percent or 400 Federal children receives payments for all such students, while a district with 2.99 percent or 399 Federally connected students receives no payments at all. Critics ask why some districts are required to "absorb" nothing, even though they may be lightly impacted and could do so if required.

In response to these criticisms, the Congress included a provision in the 1974 Amendments which, beginning in 1978, requires eligible districts to pay the full costs of educating a minimum percentage of their Federally connected children.

This "absorption" provision (Section 3(d)(2)(A) of the present law) partially reduces the inequities associated with requiring some, but not all, districts to pay for educating a minimum number of their Federal children. Although this provision is a step in the right direction, restrictions placed on the way it is to be implemented will limit its effectiveness.

The following discussions examine the present absorption provision in more detail and suggest how it might be modified and strengthened. The changes we will examine seek to improve targeting of Impact Aid funds on heavily burdened districts and achieve a more equitable treatment of all districts, eligible and ineligible alike. In order to assist the reader in the analysis of these options, Figure 3 provides a brief overview of the options, noting their strengths and weaknesses in achieving reform objectives.

Absorption Reform Based on Current Law

The current absorption provision is designed to eliminate payments for a minimum number of "B" category students. The number of children for whom payments are eliminated is derived by multiplying a district's average daily attendance by one-half the percentage of "B" category students in certain Impact Aid districts. In 1976, "B" children constituted about 4 percent of total ADA in these districts, hence the absorption percentage would have been about 2 percent.

Thus, had the absorption provision been in effect in 1976, a district with an ADA of 2,500 and a "B" enrollment of 200 would have been paid for only 150 of its "B" children and would have had to absorb the full cost of 50 (i.e., 2,500 ADA x .02 = 50 "B" children to be absorbed).

As we have noted, the current provision's effectiveness is greatly restricted by several limitations. First, "A" children are excluded in computing the districts' ADA for purposes of calculating the absorption percentage. Second, the provision does not apply to districts where "B" children comprise 10 percent or more of this adjusted ADA, or where Impact Aid payments constitute 25 percent or more of the current operating budget. These exempted districts, and those Impact Aid districts with no "B" children, are also excluded when determining the average percentage of "B" children in ADA. Third, the average percentage of "B" children cannot exceed 4 percent, thus limiting absorption, which is one-half of this percentage, to 2 percent. Finally, no district is required to absorb the costs for more than 300 "B" children. These limits on the absorption assure that it will not result in the total elimination of payments for any local education agency since, by definition, Impact Aid districts must have at least 3 percent or 400 Federally connected children.

The current provision constitutes a modest cost savings measure (FY 1978 savings are estimated at about $27 million).

The savings are achieved by slightly reducing payments for "B" children in only the most lightly impacted districts, on grounds that "B" children are the least burdensome. To some extent, this absorption addresses the criticism that Impact Aid is inequitably distributed, since it reduces payments for the lowest impact districts. It also provides more consistent treatment of eligible and ineligible low Impact Aid districts by requiring both to bear the full costs of educating some Federally connected children. On the other hand, even when this absorption is implemented, 15 percent of all Impact Aid funds will be paid to over 2,000 lightly impacted districts where Federally connected children comprise less than 10 percent of total enrollment. While the current absorption is an improvement over past practices, it is not designed to result in a significantly more equitable distribution of Impact Aid dollars.

The first absorption reform option to be examined in this section builds on the current provision but removes most of the present limitations which restrict its effectiveness. Under this option, no maximum would be set on the percent or number of children for whom a district must absorb costs, and no district would be exempted from absorption (or the calculation of the absorption percentage). This option is designed to extend the application of absorption to all Impact Aid districts and to completely eliminate payments for some of the most lightly impacted.

FIGURE 3: OVERVIEW OF ABSORPTION REFORM OPTIONS Page

OPTION	DESCRIPTION	PRO/CON
1	CURRENT ABSORPTION WITHOUT LIMITATIONS	Pro o Extends absorption provision to all districts. o Reduces payments for least burdensome "B" children. o Reductions are progressive in terms of degree of impact and property wealth. o Eliminates relatively few districts (455). Con o Does not adequately adjust for burden. Overadjusts for "A" children who may represent an absorbable burden in low impact districts. o Payments will continue for many low impact districts. o Impact Aid districts will continue to receive payments for some children below the eligibility threshold.
2	BURDEN-BASED ABSORPTION -- District absorbs costs of educating a number of Federal students equal to a specified percentage of the district's non-Federal enrollment. The tier system is eliminated, and full entitlements paid for remaining Federal children.	Pro o Absorption adjusts directly for different student burdens. o By absorbing on non-Federal students, degrees of district impact are taken into account. o Eliminates payments for low impact districts and rechannels funds to moderate and high impact districts. o Simplifies program by eliminating complex tier system. o Impact Aid and non-eligible districts treated equitably. Con o Eliminates many districts (over 1,900) from the program.
2(a)	3 Percent Absorption	Pro o Effects generally progressive in terms of degree of impact. o Districts paid only for students representing above average Federal impact. Con o Overall program costs increase, since effects of absorption are not enough to offset payment at full entitlements for "B" children and public housing children. Moderately impacted districts experience large gains in payments for these children. o Although somewhat progressive with respect to effects on districts classified by property wealth, greatest increases are for high wealth districts.
2(b)&(c)	4 & 5 Percent Absorptions	Pro o Progressive in effects on districts classified by impact and property wealth. o Reduce overall program costs. Con o 5 percent absorption hurts cities the most -- reducing payments to these districts by over 30 percent.

Although this first option has the advantage of strengthening the current absorption provision, it can be criticized on several grounds. One can argue that it does not adequately adjust for differences in burden associated with particular types of children or for overall Federal impact on districts. By not requiring absorption of "A" children and excluding them from the ADA count on which the percentage of children to be absorbed is calculated, this option overadjusts for "A" children, who may well represent an absorbable burden in lightly impacted districts.

Finally, the problem remains that under this option, non-Impact Aid districts continue to pay the full costs of educating all of their Federally connected children, while many Impact Aid districts are paid for some children below the eligibiltiy threshold.

Absorption Reform Based on Federal Burden

An alternative absorption approach can be devised which more accurately adjusts for differential burden and relative Federal impact. Based on a design originally developed by Battelle, this absorption would require each district to assume the full costs for educating a number of Federal children equal to a specified percentage of its non-Federal average daily attendance (ADA).

This absorption option has several features which recommend it for further consideration. First, when total Federal ADA is calculated, the absorption adjusts directly for different student burdens by multiplying each "A" and "B" category child by his or her entitlement weight. Second, each district's non-Federal ADA is adjusted to include all non-burden students by subtracting weighted Federal ADA from total unweighted ADA. Quite simply, non-Federal ADA is inflated by that portion of Federal ADA which does not constitute a Federal burden. Finally, by absorbing on non-Federal rather than Federal students, different degrees of district impact are automatically taken into account. That is, multiplying adjusted non-Federal ADA by the absorption percentage in order to calculate the number of Federal students a district will have to absorb reduces the number of children who must be absorbed in heavily impacted districts and increases the number in lightly impacted ones.

An illustration of how this "burden-based" absorption reform works may help clarify how these various features combine to affect SAFA payments and student counts in different types of districts. For example, if absorption were arbitratily set at 3 percent of non-Federal ADA, a heavily impacted district whose total enrollment of 1,000 was comprised of 100 non-Federal students, 700 military "A" students, and 200 military "B" students

would calculate its absorption and SAFA grant in the following manner:1/

First "A" and "B" student counts would be adjusted by their entitlement weights and added together to arrive at a number of total Federal children that reflected the relative Federal burden associated with each type of student. In this instance, 700 military "A" students would be multiplied by their entitlement weight of 1, and 200 military "B" students would be multiplied by their weight of .50. These results would then be added to arrive at an adjusted Federal student count of 800 (i.e., (1)(700) + (.50) (200) = (800).

Next, these 800 adjusted Federal students would be subtracted from the district's total ADA of 1,000 to arrive at an adjusted count of 200 non-Federal students. This number is adjusted because, in addition to the actual count of 100 non-Federal students, it includes that portion of all Federal students who do not repre-

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1/ The calculation for this illustration can also be summarized as follows:

Total ADA	1,000
Adjusted "A" Military ADA (700 x 1)	700
Adjusted "B" Military ADA (200 x .5)	100
Adjusted Federal ADA (700 + 100)	800
Adjusted Non-Federal ADA (1,000 - 800)	200
Number of Children to be absorbed (.03 x 200)	6
Number of Children for Whom SAFA Payments Are Made (800 - 6)	794

sent a Federal burden (in this instance, one-half the 200 military "B" children).

Finally, the 200 adjusted non-Federal students would be multiplied by 3 percent to arrive at the number of Federal children the district would have to absorb. In this example, the district would have to assume the full costs of educating six of its Federal students (i.e., 03(200)=6), while the Federal government would pay the district its full local contribution rate for each of the 794 remaining Federal students.

A less heavily impacted district would be treated quite differently by this absorption. To take an extreme but not uncommon example, if our hypothetical district had had only 10 military "A" and 20 military "B" children, the 3 percent absorption would have been applied to a total non-Federal ADA of 980. Since the number of students to be absorbed (i.e., .03(980)= 29.4) would have been greater than the adjusted Federal child count of 20, no Impact Aid payments would have been made to the district.

Although it may not be readily apparent, this reform provision will also result in considerable program rationalization and administrative simplification. In particular, absorption of this form eliminates the need for a tier system to prorate entitlements. By reducing total program costs and by

transforming all Federal students into essentially equivalent units of burden, this absorption permits the Federal government to pay the full costs of educating all non-absorbed Federal students.1/ In addition, if the absorption percentage were set equal to or greater than the present eligibility thresholds, then the latter could be dispensed with entirely (i.e., absorption would replace or substitute for the present eligibility criteria).2/ Establishing a single eligibility/absorption threshold would have the added advantage of treating eligible and ineligible districts on a more equitable basis, because ineligible districts would no longer have to absorb the costs of educating a percentage of non-Federal children which is greater than that absorbed by eligible districts.

If one accepts the argument that Impact Aid payments should be more heavily targeted on high impact/high burden districts than on districts that are lightly impacted and can afford to pay their own way, then these results are reasonable and progressive. In effect, the absorption reform should accomplish a significant amount of fund redistribution. On the one hand, it should eliminate payments for all children in the most

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1/ This is only equitable. If school districts are required to pay full costs for a share of their Federally connected children, the Federal government should pay full entitlements for non-absorbed Federal students.

2/ The 10-child minimum would be retained, however, to prevent deminimus payments.

lightly impacted local education agencies and for some children in all but the most heavily impacted ones. On the other hand, because final payments to non-absorbed children are made at full LCR (rather than at some prorated amount specified by the tier system), many heavily and moderately impacted districts should receive more aid than they would without absorption. That is, this absorption should eliminate payments for lightly impacted districts and partially rechannel these savings to districts that are more heavily impacted and in greater need of Federal support.

Three variants of this "burden-based" absorption reform option have been examined. These variants differ only in the level of absorption each specifies. The first option sets absorption equal to 3 percent, while the second and third variants require, respectively 4 and 5 percent absorptions. These levels were selected because they provide a range of options for reducing or eliminating payments to lightly impacted districts whose percentages of Federally connected children are below or slightly above national average Federal impact. Essentially, all of these absorptions seek to establish the principle that the Federal government's responsibility "extends only to those districts with an above average Federal impact and for districts that have such an impact,...only to the costs of educating the students above that average." 1/

1/ Battelle Memorial Institute, School Assistance for Federally Affected Areas, 1969, p. 117.

The 3 percent absorption was chosen because this was approximately the national average Federal impact that was calculated using Impact Aid program child counts.[1/] The 4 percent variant is an upward adjustment introduced because our data have not permitted us to calculate average impact using Federally connected students in non-Impact Aid eligible districts. Finally, 5 percent was selected as the maximum absorption likely to improve the program's ability to target funds on heavily impacted districts. A higher absorption would probably result in unacceptably large losses for moderate and high impact districts.

Effects of Absorption Reform

The discussion thus far has focused on the conceptual justification and design of each of the absorption reforms without

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1/ On an overall national basis, the student count situation is approximately as follows:

3(a) Students (weighted.....	364,946
3(b) Students (weighted).....	930,496
Section 6 Students (weighted).....	42,000
Total Federally Connected Students.....	1,337,442
Total Students (Approximate).....	45,609,000
Percent of Non-Federal.....	3.02
Percent Federal of Total.....	2.93

Number of SAFA children based on 1976 SAFA program tapes and adjusted by entitlement weights. Total students obtained from The Condition of Education, 1977 edition, National Center for Education Statistics, p. 30

examining whether any of these options actually results in a more equitable distribution of Impact Aid funds. This section takes the analysis one step further by reviewing what happens to the distribution of program dollars when each of the reform options is implemented.

Table 17 provides a summary of the funding changes which would result from the four absorption reforms. The table shows FY 1976 Tier 2 "A" and "B" full reform payments for districts classified by degree of impact, metropolitan status, and property wealth, as well as the percentage changes in these amounts that would result from each of the four absorption reform options.

As can be seen, the first absorption reform, which removes the limitations from the current provision, reduces total funding by about 20 percent and eliminates 455 districts from the program. These changes are as large as they are primarily because the absorption percentage for the option is approximately 4.7 percent. This is more than double the current percentage and results from including all SAFA districts in the computation of average "B" impact and removing the 4 percent maximum limit on this calculation.

Savings under this option are the result of reduced payments for all classifications of districts, although the largest reductions are incurred by districts in the lightest impact categories, particularly those in the grouping with less than 5 percent Federally connected children. This lowest impact category suffers

TABLE 17: Changes in Full Reform Tier 2 A + B Payments Resulting from Alternative Absorption Reform Options

District Characteristics	FY 76 Full Reform (Through Tier 2)		Changes Incurred By Imposing Reforms							
			Current Absorp. With Limitations Removed (Through Tier 2)		No Tier Absorption Based on Federal Burden: 3 Percent		4 Percent		5 Percent	
	# of Districts (1)	A + B Payments ($ in 0000) (2)	Number of Districts Eliminated (3)	% Change in A + B Payments (4)	Number of Districts Eliminated (5)	% Change in A + B Payments (6)	Number of Districts Eliminated (7)	% Change in A + B Payments (8)	Number of Districts Eliminated (9)	% Change in A + B Payments (10)
ALL SAFA DISTRICTS.....	3,876	$ 512.33	455	- 20.26	1,953	+6.23	2,316	- 7.48	2,530	- 18.98
Percent SAFA Pupils (Unweighted)										
75 - 100	99	$ 75.73	--	- 1.21	0	+1.97	0	+1.74	0	+1.52
50 - 74	108	51.47	--	- 3.20	3	+12.64	3	+11.19	3	+9.74
25 - 49	406	132.95	--	- 8.72	17	+27.45	19	+21.37	19	+15.30
15 - 24	480	95.26	--	- 17.32	43	+29.55	56	+13.53	58	- 2.48
10 - 14	565	79.28	--	- 31.76	97	+22.11	154	- 18.50	267	- 57.00
5 - 9	1,245	49.26	--	- 48.50	829	-61.15	1,113	- 88.78	1,194	- 97.17
Less Than 5	973	28.35	455	- 83.63	964	-99.24	971	- 99.94	973	-100.00
Metropolitan Status										
Central City	252	$ 141.13	12	- 30.54	122	+19.40	139	- 7.22	161	- 30.54
Suburban	1,045	167.99	170	- 22.18	583	- 0.28	704	- 11.25	759	- 19.95
Non-Metropolitan	1,938	183.23	257	- 11.58	956	+3.31	1,135	- 3.93	1,248	- 9.68
Unclassified a/	641	19.97	22	- 10.65	309	- 5.30	338	- 10.16	362	- 14.52
Property Per Pupil b/										
Lowest Quartile	898	163.92	99	- 13.40	403	+8.90	477	+1.22	529	- 5.00
2nd Quartile	799	106.56	110	- 24.60	407	+3.91	378	- 12.90	550	- 26.84
3rd Quartile	696	73.74	111	- 27.32	389	- 3.20	454	- 18.04	509	- 29.15
Highest Quartile	673	83.90	97	- 34.45	370	+13.33	435	- 16.38	475	- 42.79

a/ These districts could not be classified by metropolitan status. However, most are small and thus like to be non-metropolitan in character.

b/ Districts are classified on the basis of within-State rankings.

SOURCE: 1976 SAFA Program Data Matched with 1970 Census (Metropolitan Status) and 1974-1975 Equalized Property Value Data (Property Per Pupil)

120.

reductions in payments of about 85 percent, including losses of 100 percent in 455 districts.

Since low impact districts frequently are metropolitan in character and are often in the top two quartiles of property wealth, large reductions for districts in these classifications are observed as well. The smaller losses in the high impact categories probably are the result of the low concentrations of "B" children in these districts.

The first absorption option is an improvement over the current provision and has several features which may make it attractive as a reform strategy. It achieves significant cost savings by spreading payment reductions across virtually all districts. In addition it is progressive, in that the largest reductions occur in the least burdened districts. Finally, since only a relatively few districts would have their payments eliminated completely, the reform has a certain amount of political appeal.

On the other hand, this option can be criticized for not adequately adjusting for Federal burden. Low impact districts with small numbers of "A" children could easily absorb the costs of educating these children. In addition, under this option, most participating districts would continue to be in the two lowest impact categories and would also continue to receive their funds in relatively small per pupil amounts.

The 3, 4, and 5 percent burden-based absorptions are significantly different from the first absorption option, particularly with respect to the way they affect participation

and payments for districts in the most heavily and lightly burdened categories.

Table 17 shows that while the first absorption reform eliminates all payments for 455 districts, the number for which payments are eliminated completely under the burden-based absorptions ranges from 1,953 (about 50 percent of all districts) under the 3 percent option to 2,530 (about 65 percent of all districts) under the 5 percent reform. Few of the districts eliminated by any of the burden-based absorptions come from the three most heavily impacted categories. Indeed, as may be seen, most of these districts are lightly impacted, with Federal enrollments of less than 10 percent. This result was to be expected. After all, a principal goal of these three reform options is to eliminate or reduce funding for districts which are not significantly burdened by Federal activities.

Although similar to each other in terms of their effect on district participation, the burden-based absorptions differ in their impacts on total program costs. Thus, while reductions under the 4 and 5 percent absorptions are, respectively, 7.5 and 19 percent, the 3 percent absorption actually increases total program costs by over 6 percent.

These funding effects are the result of two separate absorption design features. On the one hand, reductions in aid to districts occur because payments are made for fewer Federally connected children (those not absorbed). For example, in the two lowest impact categories many districts no longer receive

payments because the number of Federal children for whom costs are to be absorbed approximates and sometimes equals their total number of Federal children.

On the other hand, increases under absorption are the result of making payments for the remaining Federal children at full entitlement, rather than at Tier 2 levels. For districts in the three most heavily impacted categories, where fewer children are absorbed, the funding increases from eliminating the tier system outweigh the savings from absorption. Increases are smallest for districts in the highest impact category because many of these districts already receive full compensation for their "A" children under the current law's provision, which sets Tier 2 payments for "A" children equal to full entitlements in districts where these students constitute at least 25 percent of total enrollment.

Although all three burden-based reform options increase payments to districts in the heavy impact categories and substantially reduce or eliminate payments in the lowest impact categories, they differ in their effects on payments to moderately impacted districts (i.e., those with Federal enrollments of between 10 and 24 percent).

The 3 percent absorption increases payments to districts which are moderately impacted primarily because these districts contain many public housing and "B" category children -- children for whom full entitlements are substantially greater than Tier 2 payments. It would appear that, in these moderately impacted

districts, the 3 percent absorption does not reduce the number of children for whom payments are made enough to offset the effects of paying full entitlement for all remaining children. Thus, large increases in payments result for districts in these two impact categories. Similarly, when districts are classified by metropolitan status, cities -- which contain the majority of public housing children -- gain over 19 percent in Impact Aid funds. Since cities tend to rank in the highest property wealth quartile, it is not surprising to find that payments to these wealthy districts increase by about 13 percent.1/

In contrast to the increases resulting from the 3 percent absorption, the 4 percent absorption would reduce payments to the 10-14 percent impact category and increase payments in the 15-24 percent group. Under the 5 percent absorption, both categories would experience reductions. Apparently, these higher absorption rates more than offset the effects of paying full entitlements to districts in these categories, with the result that their payments are reduced as the absorption percentage is increased. Not surprisingly, urban and high wealth quartile districts experience payment reductions under the 4 and 5 percent options.

1/ When a 3 percent absorption is combined with the elimination of entitlements for public housing and "B" out-of-country children, the effects are similar to those of the 5 percent absorption option. Total program costs would be reduced by 22 percent; the moderately impacted categories would lose from 16 to 67 percent of their payments; city districts would experience a 51 percent reduction; and payments to top quartile districts would decrease by 69 percent.

Although all of the absorption reforms examined achieve some measure of success in reducing payments to lightly burdened districts, the burden-based reforms are the most successful at rechanneling these funds to districts which are heavily impacted. By eliminating the need for a tier system and separate eligibility requirements, they also achieve a considerable measure of program simplification and equity. Requiring that all districts absorb the costs of educating an equivalent percentage of their non-Federal children solves the problem that under the present program Impact Aid districts are paid for all of their Federal students (even those below the eligibility threshold), while non-Impact Aid districts receive nothing. Assuming full local costs for all non-absorbed Federal students, rather than only a portion of these as determined by the tier system, reaffirms the Federal government's commitment to pay a fair share of the burden it created.

As a practical matter, however, the burdened-based absorptions do have one major drawback. Specifically, their benefits are achieved by eliminating many districts from the program, something the first option does not do. Indeed, in this respect, the first option is the most acceptable reform examined, even though it has few of the administrative and equity properties which recommend the three burden-based reforms. If saving districts is a major selection criterion, then retaining the current absorption without its restrictions is the most viable reform option we have examined.

Modifications to Improve Coordination with State Equalization Efforts

Previous sections have identified several ways in which the Impact Aid program may interfere with State efforts to equalize school finance. In a few States the net effect of the program actually is disequalizing -- 95th to 5th percentile disparities after SAFA payments are larger. In these cases, the cost for the State achieving a given degree of equalization is increased correspondingly, which means that Federal and State dollars are pulling in opposite directions. In other States the program has an equalizing effect, but this effect is so modest that is is almost imperceptible. This is because almost as many funds are distributed to high revenue districts as are distributed to low revenue districts. Finally, the program effectively interferes with equalization efforts by barring all but a few States from offsetting SAFA payments to high wealth districts.

In this section we will concentrate on reform options designed to moderate the prohibition against State offsetting under conditions that contribute to further equalization (see Figure 4 for an overview of these options). Clearly, a solution to this general problem will provide relief in those few States where Impact Aid presently is disequalizing and will serve to advance further the cause of equalization in other States.

Figure 4: Equalization-Related Options

Option	Basic Features	Advantages	Disadvantages
Option 1: EXTEND CURRENT EXCEPTION PROVISION	Permits offsetting in proportion to how closely the State approximates Federal equalization standards	o Recognizes differences of degree among States below the present equalization threshold	o Federal standards are open to criticism o May be regressive with respect to low wealth districts
Option 2: ELIMINATE FEDERAL EQUALIZATION TESTS	Permits offsetting in proportion to the portion of each district's local revenues that is equalized under the State's program	o Dispenses with Federally prescribed standards o Fully consistent with State equalization efforts	o Extent of offsetting not limited by degree of overall equalization o Low-wealth districts could lose in States with inadequate plans
Option 3: PERMIT OFFSETTING FOR HIGH WEALTH DISTRICTS	Maximum offset rate is based on the equalized portion of local revenues and applies to districts at 125 percent or more of average wealth, with proportionate reductions for districts in the range 101 to 124 percent	o Provides a graduated approach based both on district wealth and overall levels of equalization in each State o Limits offset to high-wealth districts	o Prevents equal treatment of low-wealth districts in highly equalized States

Option 1: Extension of the Current Exception Provision

The first option to be examined would extend the current exception provision to allow States which have achieved significant equalization, but do not meet the strict qualifying tests, to offset a portion of Impact Aid payments. Under this reform, the amount of Impact Aid which a State could substitute for its own equalization aid would depend on the extent to which the State has equalized expenditures. States which attain or surpass current Federal equalization standards would continue to implement the present provisions for counting Impact Aid as local revenues. A State falling outside the Federal standard would count a lesser portion of its Impact Aid payments corresponding to the degree of the State's departure from the Federal standard.

For instance, under this option a State with a disparity ratio within the current 25 percent limit would still be eligible for the maximum offset. Proportional reductions from the maximum offset would occur for States with disparity ratios between 25 and 50 percent. A State with a ratio that was greater than 50 percent, or double the present limit, would still be ineligible to count Impact Aid. Based on current information about within-State disparities, this graduated cutoff provision would extend eligibility to nine States that otherwise would not be eligible.

This option responds to the criticism that the current tests are too restrictive and do not recognize the efforts of States which have achieved a substantial degree of equalization, but still fall outside the cutoffs established by current Federal criteria. Under the present law, States which nearly meet the criteria (e.g., a State where spending disparities among the 5th and 95th percentiles are 30 percent, rather than 25 percent needed to qualify) are treated the same as those which have not made any attempt to equalize, and may have disparities of as much as 200 percent between high and low resource districts.

This option, however, provides an imperfect solution. It would require continued reliance on Federal standards to determine the degree of equalization achieved by the State. These standards have been criticized on the ground that they are based on questionable assumptions as to the proper goals and methods for achieving equalization. Currently, there is little consensus as to what are the most appropriate goals and methods. Consequently, some view Federal standards as a first step toward dictating how the States should equalize.

Perhaps the strongest criticism of this option is that it fails to protect the interests of resource poor districts within States which have inadequate equalization plans. Reductions in State aid for even a portion of the Impact Aid payments to low resource districts would reduce revenues where they already are at critically low levels.

Option 2: Elimination of the Federal Equalization Tests

Option 2 would entirely eliminate the Federal tests for determining whether a State's program is sufficiently equalized to qualify for the exception and be permitted to count Impact Aid as local revenues. All States with an equalization plan (i.e., currently all but one State) would be permitted to count Impact Aid as local revenue. This option would retain the proviso that limits the share of Impact Aid which a State can count to the proportion of locally raised revenues covered under the State equalization plan. Under this option the Federal government would no longer set standards for State equalization programs, a process which has proved to be very difficult and controversial.

This approach is intended to assure that Impact Aid districts are treated in the same manner as non-Impact Aid districts under the State's equalizing plan. Permitting the State to count Impact Aid payments in the same proportion as it counts local revenues under the State plan provides an approximation of the way revenues would have been treated if the local district had been able to tax Federal property. In effect, this option would permit a State to redirect its resources away from high wealth districts, thereby improving equalization.

States which have enacted extensive equalization plans covering the largest portion of locally raised revenues would be

able to substitute the greatest fraction of Impact Aid for State Aid. To the extent that highly equalized States would benefit most under this option, it could be veiwed as encouraging States to equalize.

Although it would reduce interference of Impact Aid payments with State efforts to equalize, this option can be criticized on several grounds. In particular, although both Impact and non-Impact Aid districts might be treated equally under the State plan, this similar treatment could be disequalizing in States with weak programs.

As in the case of Option 1, a disequalizing effect would result from taking away Impact Aid payments to low resource districts which are inadequately served under the State plan. Unlike Option 1, the State offset is not directly diminished for departures from equalization. As the data provided in Table 11 (page 60) indicate, approximately 53 percent of Impact Aid districts rank in the lowest two quartiles in terms of revenues per pupil. These districts receive about 61 percent of all Impact Aid funds. In such districts, the Federal payments, if offset by reduced State aid, would fail to provide either adequate compensation for burden or improved equalization.

Critics of this option will also question whether treatment of Impact Aid payments under the State plan would be equivalent to the treatment of revenues that a district would have raised if the Federal property were taxable. As our evaluation of the

program demonstrates, Federal Impact Aid payments may not be a good indicator of what local revenue-raising ability would be if Federal property were taxable, or what it would have been in the absence of the local Federal activities. In addition, even if a district raised the additional revenues as opposed to receiving Impact Aid, it does not follow necessarily that State payments would be reduced. For instance, States may guarantee a minimum level of aid to all districts. Thus in high wealth districts receiving the minimum level of State aid, additional local revenues would not result in reduced State aid.

Option 3: Wealth-Related Option

This third equalization option directly addresses the problem of Impact Aid payments which increase the resources of already wealthy districts. The current qualifying tests would be replaced by a measure that permits a State to offset Impact Aid at the maximum rate (i.e., the proportion of total local revenues covered under each State's plan) for all districts 25 percent or more above average wealth in the State. Proportional reductions in the maximum allowable offset rate would be made for districts with wealth advantages in the range of 1 to 24 percent over the State average. Thus, for a district whose wealth is 10 percent above the average and where 75 percent of all its local revenues are equalized, the allowable State offset would amount to 30 percent of the district's SAFA payment (i.e., 10/25th's of 75

percent). States would not be able to count any Impact Aid as local revenues in districts of below average wealth.

Over 1,000 Impact Aid districts (about one-third of all Impact Aid districts) are above their State's average wealth and would be included under this option. More than 600 are over the 25 percent advantage level where maximum offset is permissible. If State finance systems were fully equalized then the total SAFA dollars that would be at risk in districts of above average wealth would amount to about $90 million.

Under this option, the wealth measure in the State equalization plan would be used to determine how each district ranked relative to others in the State. Although there is no uniformly applied measure of wealth (e.g., income or property valuation are two common measures), nearly all States have implemented some system for measuring the fiscal capacities of their districts. Since this option is concerned with the wealth of Impact Aid districts relative to other districts in their respective States, reliance on the State's own measure would be a reasonable solution to the problem of ranking districts based on their wealth, short of imposing a uniform Federal definition.

The threshold of 125 percent of State average wealth was selected in order to assure that reductions in State aid will not impair the district's ability to finance education. Although it is not possible to identify precisely a point above which it is certain that every district would be at a fiscal advantage in financing its education costs, it does not seem unreasonable to

assume that districts which are 125 percent of State average wealth have such an advantage. The 125 percent threshold, as opposed to a threshold set at the State average, allows districts an extra margin above the State average for differing pupil needs and greater educational service costs. Proportional reductions for districts between 100 and 125 percent of the State average wealth protect against excessive losses of State aid to districts closest to the State average. The sliding scale also avoids the inequity of substantially different treatment for districts which are very close to the 125 percent threshold.

On balance, Option 3 succeeds in meeting most of the objections that can be directed against the first two options: low-wealth districts are fully protected, States are permitted to apply their own measures of wealth, and rates of offsetting are scaled to both State equalization and relative district wealth. On the other hand, this option can be criticized as potentially disruptive of State school finance reform efforts. In particular, by preventing highly equalized States from reducing State Aid to offset Federal payments the option can upset State efforts to reduce inter-district revenue disparities. In effect, it causes total revenues in low-wealth Impact Aid districts to be much higher than those in low-wealth non-Impact Aid districts. That is, this provision can create new disparities of its own.

Given the variation among the States in the methods and goals of school finance equalization, as well as in the extent to which equalization has been achieved, fashioning a Federal policy regarding the relationship of Impact Aid to State efforts to equalize is a complicated task. The current provision, which attempts to resolve some of the problems -- if only in a few highly equalized States -- represents an improvement over the absolute prohibition against States taking Impact Aid into account when distributing their State aid. However, for the vast majority of States, many of which currently are trying to improve the ability of their aid programs to equalize educational expenditures, Impact Aid can interfere with State objectives.

If the objective of reform is to ensure that the Impact Aid program remains neutral with respect to State equalization efforts, the second option, which would eliminate the strict qualifying tests and permit virtually all States to count Impact Aid payments, goes the furthest of the three options toward achieving that goal. To a lesser extent the first option also is directed toward coordinating Impact Aid with the State plan for distributing its aid. However, if one is most concerned with assuring that Impact Aid has the effect of increasing equalization, the third option, which considers the wealth of Impact Aid districts, would be preferable. Finally, Options 1 and 3 might be considered as

a package. This combination permits the maximum Federal coordination in highly equalized States and improves equalization with respect to high wealth districts in all States.

By almost any aggregate measure, equalization-related reforms of Impact Aid provisions can exert only a modest influence on State finance. Nationally, SAFA payments amount to less than 2 percent of all current expenditures for public elementary and secondary education. Thus, the importance attached to proposals of the type just considered is largely based on principles of equity and policy concerns in the areas of Federal/State/local cooperation. At the district level, specific reform options can have a substantial effect for certain high impact districts. At State and Federal levels, the fact that program dollars may be pulling in opposite directions must be a matter of policy concern, irrespective of the absolute magnitude of the amounts involved. For both of these reasons, equalization-related reforms are deserving of serious consideration.

IV. COMPREHENSIVE OPTIONS

The preceding section examined the independent effects on funding and district participation of several solutions to problems presently besetting the Impact Aid program. This concluding section essentially repeats that analysis for different combinations of these options. The combinations we examine illustrate what happens when a number of current program provisions are modified simultaneously to address the major issues raised throughout the report. In effect, we have sought to design several comprehensive reform packages which move in the direction of improving the program's ability to equitably compensate districts for genuine Federal burden.

Six design principles have guided our selections. These principles, or reform goals, generally describe our point of view concerning the Federal role in Impact Aid and may be stated as follows:

(1) The Federal responsibility should extend only to students who represent a genuine Federal burden on the district.

(2) Methods used to calculate payment rates should be as objective as possible to minimize the likelihood of abuse. Procedures which yield unbiased approximations of what local education expenditures or revenues would have been in the absence of Federal impact are to be preferred over others.

(3) Heavily impacted districts have a more valid, higher priority claim on scarce Federal resources than lightly impacted districts.

(4) Impact Aid payments should not interfere with State equalization programs.

(5) Program operations should be rationalized and simplified.

(6) Insofar as they occur, fund reductions from reform should be progressive in terms of district burden.

As will become clear, each of the reforms presented here emphasizes some principles more than others, and none is optimal from all standpoints. Any final selection from among these options must therefore depend upon the importance each reader places on these different goals and his judgment regarding each proposal's ability to attain them. For the most part, our intention has been to demonstrate that major problems can be addressed in a variety of ways, not to present a set of definitive program reforms. In effect, because they differ in terms of the number of districts they eliminate, their cost implications, and the extent to which they depart from current practices, these three options illustrate a range of plausible strategies for addressing the principles and reform goals we have described.

An Overview of the Options

Figure 5 summarizes the three reform options to be considered here in terms of the elements each uses to address the six goals or principles we have defined. As will be noted, Option 1 is a relatively conservative reform, in that it is comprised of elements which generally represent modest departures from current program provisions. Thus, while the option eliminates payments for low burden out-of-county "B" children, it continues to compensate districts for public housing students who arguably are not even Federally connected. Similarly,

FIGURE 5 : Overview of Comprehensive Reform Proposals

Comprehensive Reform Option	DESCRIPTION OF REFORM ELEMENTS DESIGNED TO ADDRESS: Reform Goal 2: Children for Whom Payments Are Made	Reform Goal 2: LCR Reform	Reform Goal 3: Districts for Whom Payments Are Made	Reform Goal 4: Coordination With State Equalization Programs	Reform Goal 5: Administrative Simplification	Reform Goal: 6 Progressive Cost Reductions	Remarks
1	Eliminate Payments for out-of-county "B" category children.	"Clean Up" comparable district method & restrict use to heavily impacted districts. All other districts use greater of 1/2 U.S. or State avg. expenditures per pupil.	Retain current absorption provision without limitations.	Implement wealth-related equalization provision.	None	Reductions are progressive on percent Federal students & wealth but cities lose about 38% of their funds.	Most modest departure from present program. Achieves reasonable cost savings without eliminating massive numbers of districts. However, reform will not go far enough for critics. LCR reform is especially weak element of this proposal. Option achieves no administrative simplifications.
2	Eliminate payments for out-of-county "B" children. Eliminate payments for public housing children.	"Clean Up" comparable district method & restrict use to heavily impacted districts. All other districts use 1/2 their St's. average expenditures per pupil.	Implement 3% No tier burden-based absorption, i.e., absorption at national average.	Implement wealth-related equalization provision	Eliminates tier system	Reductions are progressive on percent Federal students & wealth, but cities lose over half their funds.	Intermediate level reform which achieves moderate savings. Reform eliminates payments for both major categories of low burden-children, while burden-based absorption reduces or eliminates payments for many light-moderate impact districts. Heavily impacted districts are relatively untouched by reform. LCR reform improves over Option 1, but still results in imperfect rates. Administrative simplification results from elimination of Tier system. Reform may be too harsh for some, as it eliminates over 2,400 districts.
3	Eliminates payments for out-of-county "B" children. Eliminates payments for public housing children.	Eliminate comparable district method entirely: Calculate LCR based on State's locally-derived expenditures per pupil or 1/2 State average expenditures per pupil, whichever is greater.	Implement 5% No Tier burden-based absorption.	Implement wealth related equalization provision	Eliminate tier system & comparable district method.	Disregarding effect of option on one district, reductions are progressive on percent Federal children and wealth but cities lose almost 70% of their funds.	Major reform which achieves large savings. Eliminates payments for both major categories of low burden children and 5 percent absorption. Eliminates all payments to districts in lowest impact category. Disregarding affect on one district, districts in top 2 categories of impact lose less or gain compared with Option 2. LCR reform is strongest of all examined. Significant administrative simplification results from eliminating comparable district method and tier system. Reform too harsh for many and probably most controversial.

although Option 1 restricts use of the comparable district method to heavily impacted LEA's, it retains the current national average method, a procedure that is subject to some of the same problems which beset the comparable district method and one that yields equally poor approximations of the local Federal burden.

Although Option 1 accords heavily impacted districts higher priority than lightly and moderately impacted ones, it does so by retaining the current program's absorption provision without its present limitations. While eliminating these restrictions is an improvement, the resulting arrangement still constitutes an unsatisfactory way to adjust for differential Federal burden. For example, lightly impacted districts whose Federal enrollments are comprised entirely of "A" children will not have to absorb costs for any of these students, because the current absorption is taken only against "B" children. On the other hand, similar districts which just barely fail to meet the program's eligibility requirements will continue to assume the full costs of educating all of their children.

Like the two remaining options, Option 1 specifies implementation of a new wealth-related equalization provision similar to the one described in Section III. Although data limitations prevent us from determining the net effects of this provision on total district revenues, we have included it in all of the reform packages to emphasize our concern that Federal programs

be better coordinated with State finance reform efforts. This provision represents the one major departure from current practice that may be found in Option 1.

Compared with Option 1, Options 2 and 3 represent more drastic departures from the present program. Option 2 is an intermediate level reform. Like the first option, it includes a wealth-related equalization provision and eliminates payments for out-of-county "B" children. In addition, however, the option accords low burden districts and children less importance than Option 1. It does this by eliminating payments for public housing children and by implementing a 3 percent burden-based absorption which reduces payments to districts in the lowest impact category.

Option 2 extends the first reform's LCR provision by eliminating use of the national average minimum. As we have already noted, the national average calculation yields as poor an estimate of local burden, and is as subject to overpayment, as any method used. Although the State average calculation is far from perfect (for reasons we have detailed in earlier sections), it does at least conform with what we know about national average State/local expenditure patterns. Admittedly, taking one-half of each State's average per pupil expenditures yields a gross estimate of district burden. However, as gross estimates go, this one is less subject to manipulation than the comparable district method and is to be preferred to taking one-half of national non-Federal expenditures per pupil.

Option 3 constitutes the most far-reaching reform examined. Building on changes introduced by its predecessors, Option 3 would deal with the issue of Federal/State coordination by implementing a wealth-related equalization provision. Like Option 2, it would also prioritize funding by eliminating payments for low burden out-of-county "B" and public housing children.

Option 3 differs from its predecessors primarily in terms of the absorption and LCR reforms it specifies. As may be seen, Option 3 would increase the second reform's 3 percent absorption and impose a strong 5 percent provision in its place. While the general form of these two absorptions is identical, the 5 percent provision eliminates all payments currently received by districts in the lowest category of impact and reduces payments to other lightly and moderately impacted categories. In effect, this strong absorption provision fully implements the principle that the Federal government's responsibility extends primarily to districts which are most heavily burdened by Federal activities. As was noted in a previous section, this provision actually increases payments to districts in the three highest impact groupings. This is because the form of the provision specifies that payments for all remaining (i.e., non-absorbed) children be made at full entitlement rather than at some prorated tier amount.

In certain respects Option 3 comes closest of all reforms to addressing the objectives established for payment rate calculations. As may be seen from Figure 5, the option would eliminate the comparable district method entirely and replace it with a rate based on each State's actual locally derived expenditures per pupil. Alternatively, districts would be permitted to calculate their compensation using the preceding option's rate of one-half State expenditures per pupil.

The advantages and disadvantages of this calculation arrangement have been dealt with earlier. At this point it seems sufficient to note that paying on the basis of each State's average local expenditures yields estimates of local Federal burden that, on average, are at least as reasonable as those generated using present procedures. The reform method has the added advantage of being relatively straightforward and free from manipulation and abuse.1/

1/ Within-State adjustments for special district circumstances might improve this reform and make it more acceptable to high cost districts, especially those which serve the center cities. Essentially, an improvement of this sort would require that a suitable substitute for the comparable district method be identified -- one that permits rates to vary based on within-State cost of education differences. Unfortunately, there is little concensus among experts about whether or how such adjustments should be made for unimpacted districts, much less impacted ones. As a result, we have tabled this issue for future study. In the end, this problem may be moot. Center city districts are predominately lightly impacted, with Federal enrollments comprised principally of public housing children who are arguably not Federally connected to begin with. Consequently, any reform that aims to accomplish significant reductions in payments for low burden students and districts is also likely to eliminate a disproportionate number of cities from the program, regardless of how local contribution rates are calculated.

Thus far our discussion has examined the three reform packages primarily in terms of how each addresses the first four reform goals. As we have seen, all options are comprised of elements which deal with these objectives, but each differs in terms of the extent to which it does so by departing from current practice. Thus, Option 1 is a relatively conservative package that tries to bring about change by staying pretty much within the confines of the present program, while Options 2 and 3 go beyond the current set of arrangements and introduce radically new reforms affecting the types of children and districts for whom payments are made and the way these payments are calculated. In addition, it should be noted that Options 2 and 3 also differ from Option 1 because they bring about significant administrative simplification by eliminating the tier system (Options 2 and 3), and the comparable district calculation method (Option 3).

The sixth goal set for each of these reforms specifies that they reduce costs in as progressive a manner as possible with respect to district burden. Assessing whether they accomplish this purpose is the topic of the following section, which examines each option's effects on funding and district participation.

Effects on Funding and District Participation[1/]

Table 18 shows the impacts on funding and district participation of each of the three reform options. As may be seen, the

1/ Baseline comparisons in this section are made against FY 1976 full reform Tier 2 "A" and "B" payments only.

TABLE 18: Changes in Full Reform Tier 2 A and B Payments Resulting from Alternative Comprehensive Reform Options

District Classification	FY 1976 Full Reform (Through Tier 2)		Changes Incurred By Imposing Reforms: Comprehensive Reform 1		Comprehensive Reform 2 c/		Comprehensive Reform 3	
	Number of Districts (1)	A + B Payments (2)	Number of Districts Eliminated (3)	% Change in A + B Payments (4)	Number of Districts Eliminated (5)	% Change in A + B Payments (6)	Number of Districts Eliminated (7)	% Change in A + B Payments (8)
All SAFA Districts	3,876	$ 512,336.62	1,012	- 27.95	2,412	- 32.48	2,787	- 43.38
Percent SAFA Pupils								
75 - 100%	99	$ 75,730.04	1	- 0.39	1	+ 1.37	1	- 25.16 *
50 - 74%	108	51,476.38	---	- 5.35	4	+ 0.31	4	+ 2.72
25 - 49%	406	132,952.73	6	- 14.86	28	- 5.73	37	- 8.70
15 - 24%	480	95,268.97	28	- 29.78	119	- 33.42	165	- 47.85
10 - 14%	565	79,283.78	59	- 47.94	259	- 72.72	406	- 89.29
5 - 9%	1,245	49,267.90	251	- 59.17	1,037	- 85.90	1,201	- 98.02
Less Than 5%	973	28,356.78	667	- 87.66	964	- 99.37	973	-100.00
Metropolitan Status								
Central City	252	$ 141,130.16	28	- 38.06	175	- 57.44	202	- 67.10
Suburban	1,045	167,996.89	340	- 34.54	709	- 30.80	819	- 37.64
Non-Metropolitan	1,938	183,235.95	563	- 15.52	1,197	- 16.47	1,388	- 32.46 *
Unclassified a/	641	19,973.60	81	- 15.20	331	- 17.12	378	- 24.29
Property Per Pupil b/								
Lowest Quartile	898	$ 163,926.24	228	- 17.40	501	- 14.32	589	- 17.39
2nd Quartile	799	106,568.39	242	- 32.02	524	- 34.62	619	- 45.87
3rd Quartile	696	73,749.29	225	- 43.95	479	- 47.97	555	- 59.18
Highest Quartile	673	83,902.25	196	- 47.94	478	- 76.42	534	- 81.71

SOURCE: 1976 SAFA Program Data Matched with 1976 Census (Metropolitan Status) and 1974-1975 Equalized Property Value Data (Equalized Per Pupil)

* When the one large Alaskan district which dominates this category is omitted the loss to districts with 75-100 percent impact declines from -25.16 to -0.44; the loss to non-metropolitan distircts declines from -32.46 to -27.11.

a/ These districts would not be classified by metropolitan status. However, most are likely to be non-metropolitan in character.

b/ Districts classified based on within-State rankings.

c/ To simulate this option, LCR's for heavily impacted districts were retained. Even though some of these districts are not now using the comparable district method, the option gives these districts latitude to use it and thus retain or raise their current compensation levels. A more conservative methodology, which was rejected, would have assigned high impact districts not now using the comparable district method a rate equal to one-half their State's average non-Federal expenditures per pupil.

extent to which the options depart from current practices is parallelled by the degree to which each option changes overall funding and participation. For example, Option 1, conceptually the most conservative reform, also results in the most modest overall cost and district reductions. Had this option been in effect in FY 1976, total Tier 2 full reform "A" and "B" funding would have been reduced by about 28 percent, and 1,012 districts would have been eliminated from the program.

By comparison, had Option 3 been operating, FY 1976 funding would have been reduced by over 43 percent and nearly 2,800 districts (over 70 percent of all current participants) would have been eliminated. Option 2, the intermediate level reform, would have resulted in intermediate level funding reductions (about 32 percent); however, it would have eliminated 2,412 districts, almost as many as Option 3, the harshest reform examined. That Options 2 and 3 eliminate so many more districts than Option 1 may be attributed almost entirely to the different types of absorptions they specify. The reasons for these differences were noted in Section III and thus come as no surprise.

All options successfully address the sixth goal of reducing costs progressively in terms of district burden, although the heavy losses which result for districts in the highest impact category under Option 3 may give some readers pause. These losses are somewhat misleading, however, as they result because the LCR reform element in this option severely reduces payments to the

one large district that dominates the grouping. Omitting this one district from the analysis, aggregate losses to these heavily impacted districts are less than one-half of 1 percent -- a result which compares favorably with these districts' experiences under Options 1 and 2.

Disregarding the effects of reform Option 3 on this one district, our results indicate that aggregate dollar losses to districts in the top three categories of impact are lower for Options 2 and 3 than for Option 1. These results primarily reflect the effects of the two forms of absorption that have been employed. By paying full entitlements for all non-absorbed children, Options 2 and 3 apparently compensate for the fact that their absorption components require districts to assume some costs for both "A" and "B" category children. Although districts are not required to absorb "A" children under Option 1, payments are lower because they are made at less than full entitlement levels. The net effect of these differences is that, in the aggregate, payments to heavily impacted districts are higher under Options 2 and 3 than under Option 1.

The combined effect of absorption and elimination of public housing payments is the principal explanation for the larger dollar and district losses that occur to moderately and lightly impacted districts under Options 2 and 3. Although all options reduce funding to districts in these categories, clearly, Options 2 and 3 do a much better job than Option 1 of achieving the kinds of reductions and redistributions that most Impact Aid critics call for.

The progressive pattern of changes that is observed for districts classified by percent of Federal children is repeated for districts classified by property wealth. That is, payment reductions increase as district wealth increases. Although losses to districts in the lowest wealth quartile are more or less the same under all of these options (i.e., between 16 and 17 percent), losses to districts in the wealthiest quartile are much higher under Options 2 and 3 than under Option 1. These different results may once more be attributed primarily to the combined effect which burden-based absorption and elimination of public housing have on payments to high property wealth districts. As will be noted, similar differences may be observed when the three options' effects on relatively high property wealth center city districts are compared.

Our findings result in several conclusions regarding the pitfalls and problems which confront those who would attempt to improve the Impact Aid program's ability to equitably compensate districts for genuine Federal burden.

Though it is perhaps obvious, one point needs to be made before all others: Impact Aid reform which adheres to the principles we have defined will reduce or eliminate payments for many districts. There is absolutely no way to accomplish meaningful reform and maintain the status quo, because the majority of current

program recipients are not significantly burdened. As we have seen, even a relatively modest reform like Option 1 reduces funding and participation by substantial amounts. Moving to reforms which adhere more assiduously to the principles we have described results in even larger reductions and eliminations. Thus Option 3, which comes closer than any reform to achieving all of the goals we have established, also results in the largest funding reductions and district eliminations. Practically speaking, the most theoretically "pure" reforms may also be the least politically acceptable options.

A second lesson to be learned from our analysis is that reforms which seek to sharpen the program's ability to target genuine Federal burden will generally have an adverse effect on some types of districts and children who have a legitimate claim on other categories of Federal assistance. For example, while center cities are not burdened in an Impact Aid sense and hence do poorly under all of our reforms, they do have other critical educational problems which need attention. Similarly, although public housing children do not, in our opinion, represent a valid Impact Aid concern, many are educationally disadvantaged and thus have a valid claim on other types of Federal assistance. Because Impact Aid has never really been equipped to deal with these kinds of problems, other vehicles which can address these concerns need to be devised; or, if such vehicles already exist, they should be more effectively exploited. Expecting Impact Aid

to continue to do this kind of double and triple duty is unrealistic and inconsistent with both the program's principal purposes and the reform objectives we have set.

Finally, although we have attempted to be as thorough as possible in our analysis and explore as wide a range of elements and options as we could, areas exist where further study is warranted. In particular, additional investigation of alternative methods for gauging the net effect of Federal activities on district resources would be most helpful and could result in more equitable compensation schemes than we have devised.

Further investigation of the types of children for whom payments are made is also needed. For example, the extent to which payments are made for children whose parents work on Federal property in another district but not in another county should be determined, since these payments are as difficult to justify as those which are made for out-of-county "B" children.

Last, more information is needed about the effects which more flexible Impact Aid equalization provisions will have on total district revenues. Because improved coordination between State equalization reform and Federal funding is a topic which transcends the Impact Aid program, research might have particularly large payoffs. It might even result in Federal programs which are designed to facilitate State reform efforts.